Supreme Court, U.S.
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No. _____

IN THE
Supreme Court of the United States

COUNTY BANK OF REHOBOTH BEACH, DELAWARE AND MAIN STREET SERVICE CORPORATION,

Petitioners,

v.

JALIYAH MUHAMMAD,

Respondent.

On Petition for a Writ of Certiorari to the Supreme Court of New Jersey

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PETITION FOR A WRIT OF CERTIORARI

Claudia Callaway*
Michael M. Berger
Sabrina M. Rose-Smith
Manatt, Phelps & Phillips, LLP
700 12th Street, NW
11th Floor
Washington, DC 20005

Counsel for Main Street Service Corp.

Marc J. Zucker
Susan Verbonitz
Weir & Partners LLP
Suite 500
The Widener Building
1339 Chestnut Street
Philadelphia, PA 19107

Counsel for County Bank of Rehoboth Beach, Delaware

****Counsel of Record***

QUESTIONS PRESENTED

This case, in which the New Jersey Supreme Court determined that the class arbitration waiver contained in the parties' arbitration agreement was unconscionable and unenforceable because the Respondent's claim was a "low value" consumer claim, presents the following three questions:

- Whether the New Jersey Supreme Court erroneously ruled – in conflict with the Federal Arbitration Act, this Court's precedents and multiple state courts and federal courts of appeal – that a class arbitration waiver in an otherwise enforceable arbitration agreement is unenforceable and must be stricken;

- Whether the New Jersey Supreme Court's ruling violates Petitioners' right to due process because it applies a new interpretation of New Jersey law retroactively to the parties; and,

- Whether the New Jersey Supreme Court's ruling unduly burdens interstate commerce by seeking to impose special requirements on arbitration agreements that are contrary to the Federal Arbitration Act.

PARTIES TO THE PROCEEDING AND RULE 29.6 STATEMENT

Petitioners County Bank of Rehoboth Beach, Delaware and Main Street Service Corporation were defendants, appellees and respondents below. Easy Cash and Telecash, named as defendants, appellees and respondents below, are trade names of County Bank and not listed here.

Respondent Jaliyah Muhammad was plaintiff, appellant and petitioner below.

Pursuant to S. Ct. Rule 29.6, Petitioners state that there is no parent or publicly held company that owns 10% or more of the stock of County Bank of Rehoboth Beach, Delaware or Main Street Service Corporation.

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County Bank of Rehoboth Beach, Delaware ("County Bank") and Main Street Service Corporation ("Main Street") respectfully petition for a writ of certiorari to review the judgment of the New Jersey Supreme Court in this case.

OPINIONS BELOW

The opinion of the New Jersey Supreme Court entitled *Muhammad v. County Bank et al.*, is not yet reported (although it is available at 2006 WL 2273448) and reprinted in the attached Appendix A ("App."). The order of the New Jersey Supreme Court denying reconsideration of its decision is unreported and reprinted at App. E. The opinion of the New Jersey Superior Court, Appellate Division is reported at 379 N.J. Super. 222 (2005) and reprinted at App. B. The New Jersey Superior Court Trial Division's order granting the Petitioners' Motion to Stay Action Pending Arbitration and Compel Arbitration is unreported and reprinted at App. C.

JURISDICTION

The New Jersey Supreme Court issued its decision on August 9, 2006. App. A. The court denied rehearing on October 5, 2006. App. E. Petitioners invoke this Court's jurisdiction pursuant to 28 U.S.C. § 1257.

CONSTITUTIONAL AND STATUTORY PROVISIONS INVOLVED

The Supremacy Clause of the United States Constitution, U.S. Const., art. VI, cl. 2:

> This Constitution, and the Laws of the United States which shall be made in Pursuance thereof; * * * shall be the supreme Law of the Land; and the Judges in every State shall be bound thereby, any Thing in the

Constitution or Laws of any state to the Contrary notwithstanding.

The Fourteenth Amendment to the United States Constitution, U.S. Const. amend. XIV, § 1:

> No State shall make or enforce any law which shall abridge the privileges or immunities of citizens of the United States; nor shall any State deprive any person of life, liberty, or property, without due process of law; nor deny to any person within its jurisdiction the equal protection of the laws.

The Commerce Clause of the United States Constitution, U.S. Const. art I, sec. 8, cl. 3:

> The Congress shall have power * * * To regulate Commerce with foreign Nations, and among the several States * * *

Section 2 of the Federal Arbitration Act, 9 U.S.C. § 2 ("FAA"):

> A written provision in any * * * contract evidencing a transaction involving interstate commerce to settle by arbitration a controversy thereafter arising out of such contract or transaction * * * shall be valid, irrevocable, and enforceable, save upon such grounds as exist in law or equity for the revocation of any contract.

INTRODUCTION

Muhammad presents three constitutional issues, one of which has sharply split multiple state and federal courts, while the other two are challenges to long established commerce clause and due process principles.

First, if the terms of the agreement to arbitrate expressly preclude class procedure, can a state court alter that agreement in any way? Is such a ruling preempted by the FAA? This Court posed these questions without answering them in *Southland Corp. v. Keating*, 465 U.S. 1 (1984), and the time is now right for an answer.

Second, this Court disfavors retroactivity in the law. Ignoring this Court's precedent, the New Jersey Supreme Court applied a new interpretation of its law retroactively, imposing its new interpretation on parties previously in compliance with both New Jersey law as it existed at the time of their contracts and Delaware state law, which the parties chose as governing law in their agreement. The unconstitutionality of New Jersey's retroactive application of the law requires this Court's review.

Third, the Constitution vests power to regulate interstate commerce in Congress. State regulation of interstate commerce must yield to Congress' expressed intent, yet New Jersey will not. *Muhammad's* holding imposes far-reaching burdens on interstate commerce where Congress has clearly expressed its intent that arbitration clauses in contracts affecting interstate commerce be favored, rather than burdened.

These issues need certiorari review now.

- **The Circuits and the States are split. S. Ct. Rule 10(b).**

The New Jersey Supreme Court joins California and the U.S. Courts of Appeal for the First and Ninth Circuits as jurisdictions choosing to treat arbitration agreements in "low value" cases differently than other contracts. As discussed below at pp. 15-17, these jurisdictions have held that the class action waivers included in arbitration agreements are

unenforceable in low value consumer cases. In contrast, many state and federal circuits hold either that courts may not order class wide arbitration unless the parties have so agreed, or that, if the parties have agreed not to arbitrate as a class, the contract between the parties is not unconscionable.

The Seventh Circuit, for example, has held that courts are without authority to order class-wide arbitration unless the parties have expressly agreed to that procedure. *Champ v. Siegel Trading Co.*, 55 F.3d 269, 276-277 (7th Cir. 1995). The Third, Fourth, Eighth, and Eleventh Circuits—unlike the New Jersey Supreme Court—have enforced arbitration agreements despite the unavailability of class action procedures under those agreements.[1] The decision below likewise conflicts with the decisions of the Second, Fifth, Sixth, Eighth, and Eleventh Circuits, all of which have reached the related conclusion that the FAA precludes courts from requiring consolidation of arbitration proceedings unless the parties expressly agreed to do so in their arbitration agreements.[2]

- **The New Jersey ruling directly conflicts with the decisions of this Court. S. Ct. Rule 10(c).**

This Court often has admonished that arbitration agreements must be enforced according to their terms—even in more drastic cases, such as when enforcement of the agreement results in piecemeal litigation of the contracting parties' claims or an order to compel arbitration of a contract

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[1] *Snowden v. Checkpoint Check Cashing*, 290 F.3d 631, 638-639 (4th Cir. 2002), *Dominium Austin Partners, L.L.C. v. Emerson*, 248 F.3d 720 (8th Cir. 2001); *Randolph v. Green Tree Fin. Corp.*, 244 F.3d 814, 817-818 (11th Cir. 2001); *Johnson v. West Suburban Bank*, 225 F.3d 366, 369 (3d Cir. 2000), cert. denied, 531 U.S. 1145 (2001).

[2] *See* pp. 15-16, below.

that is eventually determined to be void *ab initio*. This Court previously has recognized that an arbitration agreement may be enforced "even if the arbitration could not go forward as a class action. . ." *Gilmer v. Interstate/Johnson Lane Corp.*, 500 U.S. 20, 32 (1991) (internal quotation omitted). The New Jersey ruling conflicts with this Court's application of the FAA.

A plurality of this Court also stated in *Green Tree Financial Corp. v. Bazzle*, 539 U.S. 444 (2003), that where an arbitration agreement is silent as to whether the parties consent to class arbitration, an arbitrator must decide that issue. The Court's ruling implies that parties are free to permit or prohibit class arbitration. It would be improper, then, to strike the parties' statement of intent from the arbitration agreement, yet the New Jersey Supreme Court decision does so, interfering with the parties' right to contract according to their own terms. As the late Chief Justice Rehnquist, joined by Justices O'Connor and Kennedy in his dissent in *Bazzle*, stated, a state supreme court decision imposing class arbitration upon parties who impliedly provided otherwise "imposed a regime that was contrary to the express agreement of the parties" and thereby violated the FAA. 539 U.S. at 459 (Rehnquist, C.J., dissenting).

The Court also has held that a new law, or new interpretation of an existing law, should be applied only prospectively. *Bowen v. Georgetown Univ. Hospital*, 488 U.S. 204, 208 (1988) ("Retroactivity is not favored in the law."). The New Jersey Supreme Court applied its "low value" distinction to arbitration agreements which, prior to its ruling, had not been unconscionable. Because this Court has held that a court may not automatically apply a change in the law retroactively where the application of that law attaches new legal consequences to completed, past conduct that was legal at the time, see *Usery v. Turner Elkhorn*

Mining Co., 428 U.S. 1, 15-16 (1976), the New Jersey ruling conflicts with this Court's precedent.

- **The conflict concerns a matter of overriding national importance. S. Ct. Rule 10(c).**

The New Jersey Supreme Court's decision in this case contravenes the central purpose of the FAA: enforcing arbitration agreements according to their terms. The conflict between New Jersey's new law and that of the majority of states has nationwide implications. Tens of thousands of standard commercial and consumer contracts contain arbitration provisions. In most of the rest of the country, courts enforce arbitration agreements as written, declining to rewrite them either to exclude an agreed upon class action waiver or include a class procedure to which the contracting parties did not agree. Thus, parties to standard contracts containing standard arbitration provisions face the prospect of starkly different proceedings arising from those contracts—all depending on whether they sue or are sued in New Jersey, or elsewhere.

In *Southland Corp. v. Keating*, *supra*, this Court noted probable jurisdiction to determine whether the California Supreme Court's ruling imposing a class action structure on an arbitration conflicted with the FAA. This Court concluded that it could not exercise jurisdiction over that question because it had not been raised adequately below. *Id.* at 9. The question left open in *Southland* still vexes the nation's lower courts and is squarely presented by this case. The conflict between the New Jersey Supreme Court's approach and that of most federal and state courts of appeal highlights a conflict that has only deepened in the intervening years—as is evidenced by the recent proliferation of petitions for certiorari on this and related issues. Certiorari should be granted to resolve, at last, this important question.

STATEMENT OF THE CASE

Jaliyah Muhammad ("Muhammad") sought out County Bank, a federally-insured, Delaware chartered depository institution, for a loan. App. B at 5. On or about April 28, 2003, she requested a short term, single advance, unsecured $ 200.00 loan. *Id.* at 6. To obtain the loan, County Bank's loan servicer, Main Street, faxed an application form to Muhammad, who completed, signed and faxed the completed application back to Main Street. *Id.*

After County Bank approved the loan, it transmitted funds directly to Muhammad's checking account via an ACH credit entry transaction. *Id.* at 7. Muhammad repeated this process for two additional loans, one on May 23, 2003 and another on June 6, 2003, each for $200.00. *Id.*

Muhammad's loans are evidenced by Note and Disclosure Statements ("Notes"). *Id.* The Notes clearly identify County Bank as the lender, a fact which Muhammad does not dispute. *Id.* at 5. Like the loan application, the Notes were received by facsimile, signed by Muhammad, and returned by facsimile to County Bank's loan servicer, Main Street. *Id.* at 6. The terms of the loans are clearly and prominently set forth in the Notes, including the annual percentage rate ("APR") and finance charge. *Id.* at 7.

The Notes also contain a choice of law clause providing that Delaware law governs the agreement and the relationship of the parties, except as federal law applies. App. H at 3. In addition, each of the Notes advised

Muhammad that County Bank had retained Main Street to service her loan. App. B. at 6.[3]

The Notes contain the following binding arbitration agreement above Muhammad's signature:

> AGREEMENT TO ARBITRATE ALL DISPUTES:
> You [the borrower] and we [County Bank] agree that any and all claims, disputes or controversies between you and us and/or the Company [defined as Main Street in the Notes], any claim by either of us against the other or the Company (or the employees, officers, directors, agents, or assigns of the other or the Company) and any claim arising from or relating to your application for this loan or any other loan you previously, now or may later obtain from us, this Loan Note, this agreement to arbitrate all disputes, your agreement not to bring, join or participate in class actions, regarding collection of the loan, alleging fraud or misrepresentation, whether under the common law or pursuant to federal, state or local statute, regulation or ordinance, including disputes as to the matters subject to arbitration, or otherwise, shall be resolved by binding individual (and not joint) arbitration by and under the Code of Procedure of the National Arbitration Forum ("NAF") in effect at the time the claim is filed. . . Your arbitration fees may be waived by the NAF in the event you cannot afford to pay them. The cost of any participatory, documentary or telephone hearing, if one is held at your or our request, will be paid for solely by us as provided in the NAF Rules and, if a participatory hearing is requested, it will take place at a

[3] Muhammad listed two County Bank trade names, "Easy Cash" and "Telecash" as defendants. County Bank used these trade names in connection with the advertising and marketing of its short term loans. However, the application and Notes clearly identify County Bank as the lender and Main Street as the servicer. App. B at 6.

location near your residence. This arbitration agreement is made pursuant to a transaction involving interstate commerce. It shall be governed by the Federal Arbitration Act, 9 U.S.C. Sections 1-16. . .

App. B at 6. The arbitration agreement is followed by a notice, which appears in capital letters:

> NOTICE: YOU AND WE WOULD HAVE HAD A RIGHT OR OPPORTUNITY TO LITIGATE DISPUTES THROUGH A COURT AND HAVE A JUDGE OR JURY DECIDE THE DISPUTES BUT HAVE AGREED INSTEAD TO RESOLVE DISPUTES THROUGH BINDING ARBITRATION.

Id.

In addition, the Note contains a separate agreement not to bring, join, or participate in class actions:

> *AGREEMENT NOT TO BRING, JOIN OR PARTICIPATE IN CLASS ACTIONS:* To the extent permitted by law, you agree that you will not bring, join or participate in any class action as to any claim, dispute or controversy you may have against us, our employees, officers, directors, servicers and assigns. You agree to the entry of injunctive relief to stop such a lawsuit or to remove you as a participant in the suit. You agree to pay the attorney's fees and court costs we incur in seeking such relief. This Agreement does not constitute a waiver of any of your rights and remedies to pursue a claim individually and not as a class action in binding arbitration as provided above.

Id.

Immediately above Muhammad's signature is the following notice, again printed in capital letters:

> BY SIGNING BELOW, YOU AGREE TO ALL OF THE TERMS OF THIS NOTE, INCLUDING THE AGREEMENT TO ARBITRATE ALL DISPUTES AND THE AGREEMENT NOT TO BRING, JOIN OR PARTICIPATE IN CLASS ACTIONS. YOU ALSO ACKNOWLEDGE RECEIPT OF A FULLY COMPLETED COPY OF THIS NOTE.

Id. at 6-7.

Although Muhammad agreed to arbitrate disputes and not to bring, join or participate in class actions, she filed a putative class action in New Jersey state court. *Id.* at 7. Arguing federal preemption, Petitioners timely removed the action from state court to federal court, but the case was remanded in June, 2004. *Id.*

The New Jersey Superior Court's Trial Division granted Petitioners' motion to stay proceedings and compel arbitration, after reviewing New Jersey case law and finding that, although the arbitration agreement was an adhesion contract, it could be enforced, including the class action waiver it contained.

The Superior Court's Appellate Division heard Muhammad's appeal and again ruled in favor of enforcing the arbitration agreement. The Appellate Division analyzed the plaintiff's unconscionability challenge in light of the four factors set forth by the New Jersey Supreme Court in *Rudbart v. North Jersey Dist. Water Supply Comm'n*, 127 N.J. 344, 353, 605 A.2d 681 (1992). Balancing the strong federal and New Jersey state policy favoring arbitration, the appellate court determined that the arbitration agreement was enforceable as written.

Rejecting plaintiff's argument that the class action waiver itself made the arbitration agreement unenforceable, the Appellate Division relied on *Gras v. Associates First Capital Corp.*, 346 N.J. Super. 42, 47, 786 A.2d 886 (App.Div. 2001), cert. denied, 171 N.J. 445, 794 A.2d 184 (2002), which had held that an arbitration agreement precluding class actions was not void as against the public policy of the state of New Jersey.

The New Jersey Supreme Court granted Muhammad leave to appeal. Overturning the two lower courts, the New Jersey Supreme Court found that an arbitration agreement containing a class action waiver was unconscionable and thus unenforceable in cases where small value claims might be brought.

The court distinguished *Gras* based on the fact that Muhammad's claim was considered one of a new class of "low value" claims that triggered the state law on unconscionability. The court did not set a dollar amount or other standard for determining in future cases whether a claim was large enough for *Gras'* holding to apply (as in the *Delta Funding Corp. v. Harris*, 2006 WL 2277984 (N.J. 2006) case decided by the court on the same day and reprinted here at App. D), or small enough for its holding in *Muhammad* to apply.

BASIS FOR GRANTING THE WRIT OF CERTIORARI

I. THE COURT SHOULD GRANT CERTIORARI TO DETERMINE WHETHER THE FAA PREEMPTS STATE-LAW RULES REQUIRING CLASS-ACTION PROCEDURES TO BE SUPERIMPOSED ON ARBITRATION.

Long before the state and federal conflicts over the enforceability of arbitration agreements reached as far and wide as they do today, this Court ordered briefing and argument on the question whether, if state law required "superimposing class-action procedures on a contract arbitration," it would conflict with the FAA and thus violate the Supremacy Clause. *Southland*, 465 U.S. at 8. In 1987, this Court concluded that it lacked jurisdiction to decide the issue because the appellant "did not contend in the California courts that, and the state courts did not decide whether, state-law imposing class-action procedures was pre-empted by federal law." *Id.*

Today the question is neither rhetorical nor hypothetical. The present case exemplifies the minority view on a long-simmering and important issue that now has created conflict among the states and the federal circuits. The question divides state courts within the same state, federal courts across the circuits, and even federal and state courts within the same circuit. This issue is of great importance not only to the petitioners, but also to all U.S. companies whose interaction with consumers may possibly fall within the new and nebulous sub-category of so-called "low value" claims.

Petitioners preserved this issue for review by raising the preemption argument as soon as the New Jersey Supreme Court issued an opinion contrary to the FAA. In their motion for reconsideration, Petitioners expressly questioned

whether the New Jersey Supreme Court's ruling was preempted in a motion for reconsideration. The motion for reconsideration is reprinted at App. F.

A. The New Jersey Supreme Court Ruling Conflicts With The Decisions Of Multiple Other Federal And State Courts, Including The Third Circuit.

The New Jersey Supreme Court's ruling that an arbitration agreement containing a class waiver is unconscionable in "low value" cases conflicts with other courts that have considered the issue. Among the state courts, California also has determined that an otherwise valid arbitration agreement containing a class action waiver is unconscionable in small consumer claims. *Discover Bank v. Superior Court*, 36 Cal. 4th 148, 30 Cal. Rptr. 3d 76, 113 P.3d 1108 (2005). Supreme courts in Alabama, Illinois, and West Virginia have found arbitration clauses containing class action waivers invalid only where the arbitration clause contained other unfair provisions, such as limitations on claims, causes of action, or damages.[4] Appellate courts in Florida, Missouri, and Pennsylvania also have invalidated

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[4] *See Leonard v. Terminix International Co.*, 854 So.2d 529, 538-39 (Ala.2002) (striking clause that also limited recovery of damages); *Kinkel v. Cingular Wireless LLC*, 223 Ill.2d 1, 857 N.E.2d 250, 306 Ill.Dec. 157 (2006) (clause did not contain a provision under which the company would pay arbitration costs, did not provide for recovery of attorney's fees if permitted by applicable law and limited punitive damages); *State ex rel. Dunlap v. Berger*, 211 W.Va. 549, 567 S.E.2d 265 (W.Va. 2002) (prohibiting punitive damages), *cert. denied, sub nom., Friedman's, Inc. v. West Virginia ex rel. Dunlap*, 537 U.S. 1087 (2002).

agreements where the class waiver was accompanied by unfair limits on claims and damages.[5]

Most state courts to have considered this issue have upheld arbitration agreements containing class action waivers. State courts in Illinois[6] and Texas[7] have held, like the Tennessee Court of Appeals, that, regardless of any state-law concern about "the unavailability of class action relief," "the Supremacy Clause of the Federal Constitution. . . preclude[s] [a court] from invalidating an arbitration agreement otherwise enforceable under the FAA simply

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[5] *Powertel, Inc. v. Bexley*, 743 So.2d 570, 575-76 (Fla.App.1999), review denied, 763 So.2d 1044 (Fla. 2000) (company's liability limited only to actual damages, no provision allowing injunctive or declaratory relief as provided for in state statute); *Bellsouth Mobility LLC v. Christopher*, 819 So.2d 171, 173 (Fla.App. 2002) (same); *Whitney v. Alltel Communications, Inc.*, 173 S.W.3d 300, 313-14 (Mo.App.2005) (arbitration agreement required consumer to bear own costs, making it prohibitively expensive); *Thibodeau v. Comcast Corp.*, 2006 WL 3457582 (Pa.Super. 2006)(Nos. 2176 EDA 2005, 2117 EDA 2005) (one-sided clause effectively forced consumer to arbitrate but left access to court open to corporation).

[6] *Hutcherson v. Sears Roebuck & Company*, 342 Ill. App. 3d 109, 793 N.E. 2d 886 (Ill. App. 2003), rev. denied (class action waiver is not unconscionable under Arizona law, and FAA requires class action waiver to be enforced in accordance with its terms).

[7] *AutoNation USA Corporation v. Leroy*, 105 S.W. 3d 190 (Tex. 2003) (right to arbitrate under the FAA trumps right to maintain a class action).

because a plaintiff cannot maintain a class action." *Pyburn v. Bill Heard Chevrolet*, 63 S.W.3d 351, 365 (Tenn. Ct. App. 2001).[8]

State courts in Delaware, the District of Columbia, Hawaii, Kansas, Maine, Maryland, New York, and North Dakota, have determined, like the state of Colorado, that class action waivers are not unconscionable under state law. *Rains v. Foundation Health Systems Life & Health*, 2001 Colo. App. LEXIS 580 (Ct. App. Colo. Mar. 29, 2001)(No. 99CA2398,) No. 99CA2398 ("arbitration clauses are not unenforceable simply because they might render a class action unavailable").[9]

The federal courts of appeal split along roughly the same lines. The First Circuit and the Ninth Circuit have held that arbitration agreements containing class action waivers are unconscionable. *Ting v. AT&T*, 319 F.3d 1126 (9th Cir. 2003), cert. denied, 124 S. Ct. 53 (2003) (following California Court of Appeal's opinion in *Szetela v. Discover*

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[8] The Tennessee Supreme Court denied the plaintiff's petition for review in that case and ordered the state court of appeals decision published (63 S.W.3d at 351), which means that the decision "may be relied upon by the bench and bar of [Tennessee] as representing the present state of the law with the same confidence and reliability as the published opinions of [the Tennessee Supreme] Court." *Meadows v. State*, 849 S.W.2d 748, 752 (Tenn. 1993).

[9] *See Strand v. U.S. Bank National Ass'n* , 2005 ND 68, 693 N.W.2d 918, 926 (2005); *Walther v. Sovereign Bank*, 386 Md. 412, 438-42, 872 A.2d 735, 750-53 (2005); *Brown v. KFC National Management Co.*, 82 Haw.226, 921 P.2d 146 (1996); Stenzel v. Dell, Inc., 870 A.2d 133 (Me. 2005); *Forest v. Verizon Communications*, 805 A.2d 1007 (D.C.App. 2002) (upholding validity of forum selection clause despite unavailability of class actions in that forum); *Ranieri v. Bell Atlantic Mobile*, 759 N.Y.S.2d 448, 304 A.D.2d 353, app. denied, 1 N.Y. 3d 502, 807 N.E. 2d 290 (2003); *Pick v. Discover Financial Services*, 2001 WL 1180278 (D. Del. 2001)(No. 00-935-SLR).

Bank, 97 Cal. App. 4th 1094 (2002) and holding that class action waiver is unconscionable under California law); *Kristian v. Comcast Corp.*, 446 F.3d 25 (1st Cir. 2006) (finding recovery in antitrust case so small as to make class action waiver unconscionable).

In contrast, a federal district court in West Virginia recently rejected the state supreme court's holding that arbitration provisions containing class waivers are unconscionable when the damages sought are small, finding that holding to be preempted by the FAA. *Schultz v. AT&T Wireless Servs., Inc.*, 376 F. Supp. 2d 685, 691 (N.D. W.Va. 2005).

The Fifth[10] and Eleventh[11] Circuits, while not weighing in on the preemption issue specifically, reached the same conclusion by finding that state laws conditioning the enforceability of an arbitration provision on the availability of class-wide arbitration are incompatible with the objectives of arbitration.

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[10] *Iberia Credit Bureau*, 379 F.3d 159, 174 (quoting *Gilmer*, 500 U.S. at 31) ("the fact that certain litigation devices may not be available in an arbitration is part and parcel of arbitration's ability to offer 'simplicity, informality, and expedition,' characteristics that generally make arbitration an attractive vehicle for the resolution of low-value claims.").

[11] *Caley v. Gulfstream Aerospace Corp.*, 428 F.3d 1359, 1378 (11th Cir. 2005) (quoting *Gilmer*, 500 U.S. at 31)(finding that prohibition of class arbitration is "consistent with the goals of 'simplicity, informality, and expedition' touted by the Supreme Court in *Gilmer*.").

The Second, Fourth, Sixth, Seventh, and Eighth federal Circuits have all found,[12] like the Third Circuit, that the procedural right to a class action is waivable, and that an arbitration agreement containing a class action waiver is fully enforceable. *Johnson v. West Suburban Bank*, 225 F.3d 366, 374 (3d Cir. 2000), s*ee Lloyd v. MBNA Am. Bank, N.A.*, 27 Fed. Appx. 82, 84 (3d Cir. 2002).

The *Johnson* opinion creates an extremely troubling conflict over the arbitration issue. Under *Johnson*, the class waiver in this case would be enforceable in a federal court sitting in New Jersey but, under *Muhammad*, is not enforceable in state courts there. That express conflict between the circuit and state courts invites forum shopping, and places companies in an untenable position: they cannot manage litigation risks because that risk will be solely determined by the court in which a potential case is brought.[13]

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[12] *JLM Industries, Inc. v. Stolt-Nielson SA*, 387 F.3d 163 (2nd Cir. 2004); *Snowden v. Checkpoint Check Cashing*, 290 F.3d 631, 638 (4th Cir. 2002); *Burden v. Check into Cash of Kentucky, LLC*, 267 F.3d 483 (6th Cir. 2001); *Caudle v. American Arbitration Association*, 2000 WL 1528950 (7th Cir. Oct. 17, 2000) (No. 00-1423), *In re Piper Funds, Inc.*, 71 F.3d 298 (8th Cir. 1995).

[13] This Court has long recognized that, "[i]f the federal court allows arbitration where the state court would disallow it, the outcome of litigation might depend on the courthouse where suit is brought." *Bernhardt v. Polygraphic Co.*, 350 U.S. 198, 203 (1956). The converse, of course, is equally true: Parties to a contract affecting interstate commerce may not avoid arbitration by filing their action in a state court when, had the action been brought in federal court, they would have been compelled to arbitrate. *See Burke Co. Public Sch. Board of Education v. Shaver Partnership*, 303 N.C. 408 (1981). To prevent such conflicts, Congress specifically imbued the FAA with preemptive force—where state and federal law would result in disparate rulings, the state burdening arbitration while federal law promotes it, the federal law must govern.

The forum shopping concern is only one of many reasons this issue is deeply important to companies who regularly contract with consumers. All entities, from cable and wireless service providers to finance and credit card companies, are at the mercy of state and federal courts, which may decide that the claims stemming from their service contracts are "low" enough to render their arbitration agreements unconscionable. In New Jersey alone, the issue is paramount. If a consumer with more loans than Muhammad were to bring a claim, it may or may not be large enough to merit enforceability under *Delta Funding* or *Muhammad*.

Petitioners, an out of state bank and a loan servicing company, are powerless to determine how the new rule will be applied, and even if they could determine how the New Jersey rule will be applied, they would not be able to consistently apply this rule outside of New Jersey. The New Jersey ruling forecasts 50 disparate state laws, each unique and potentially different from the law of the federal circuits sitting in those states, all amounting to a contracting and litigation nightmare for interstate commerce. Tens of millions of potential contracts, including thousands of County Bank's own agreements, are threatened as a result. *See* App. G (United States Chamber of Commerce, as *amici* to the New Jersey Supreme Court, discussing the impact on its 3,000,000 member businesses.)

B. The FAA Preempts New Jersey's Rule That Class Action Waivers Are Unconscionable In Low Value Cases.

The FAA "declared a national policy favoring arbitration and withdrew the power of the state to require a judicial forum for the resolution of claims which the contracting parties agreed to resolve by arbitration." *Southland*, 465 U.S. at 10. "[M]otivated, first and foremost, by a

congressional desire to enforce agreements into which parties had entered," the Act was passed to "ensure judicial enforcement of privately made agreements to arbitrate," placing arbitration agreements "upon the same footing as other contracts." *Dean Witter Reynolds Inc. v. Byrd*, 470 U.S. 213, 219, 220 (1985); *see Mastrobuono v. Shearson Lehman Hutton, Inc.*, 514 U.S. 52, 53-54 (1995) (Arbitration Act's "central purpose" is "to ensure 'that private agreements are enforced according to their terms' ") (quoting *Volt Info. Sciences, Inc. v. Board of Trustees of Leland Stanford Junior Univ.*, 489 U.S. 468, 479 (1989)).

To carry out the FAA's central purpose, state and federal courts are instructed to "rigorously enforce agreements to arbitrate, even if the result is 'piecemeal' litigation." *Dean Witter Reynolds*, 470 U.S. at 221 (quoting *Moses H. Cone Mem. Hosp. v. Mercury Const. Corp.*, 460 U.S. 1, 20 (1983)); *Perry v. Thomas*, 482 U.S. 483, 489 (1987). And under the Supremacy Clause, state laws in conflict with the FAA's strong policy in favor of arbitration must give way. *See, e.g., Perry*, 482 U.S. at 484 (finding preempted a California law allowing certain actions to be maintained in court " 'without regard to the existence of any private agreement to arbitrate' ") (quoting Cal. Lab. Code Ann. § 229); *Southland*, 465 U.S. at 11-12 (finding preempted a California law interpreted by state courts to require judicial consideration of claims).

In declaring class arbitration waivers unenforceable in "low" value cases, the New Jersey Supreme Court placed its own policy preference for class actions squarely above Congress's policy of ensuring the enforcement of arbitration agreements as written. *See, e.g., Mastrobuono v. Shearson Lehman Hutton, Inc.*, 514 U.S. 52, 53-54 (1995); *Volt Info. Scis., Inc. v. Bd. of Trs. of Leland Stanford Jr. Univ.*, 489 U.S. 468, 479 (1989); *Dean Witter Reynolds Inc. v. Byrd*, 470 U.S. 213, 219-221 (1985). When state and

Congressional policies clash, Congress prevails. *Perry v. Thomas*, 482 U.S. 482, 491 (1987).

This Court also has made clear that state law is preempted whenever it "stands as an obstacle to the accomplishment and execution of the full purposes and objectives of Congress." *Fid. Fed. Sav. & Loan Ass'n v. de la Cuesta*, 458 U.S. 141, 153 (1982) (internal quotation marks omitted); *see also Geier v. Am. Honda Motor Co.*, 529 U.S. 861, 869- 874 (2000); *United States v. Locke*, 529 U.S. 89, 109 (2000). New Jersey's rule conditioning enforcement of arbitration provisions on the value of the claim and whether class arbitration is permitted threatens Congress' primary objective in enacting the FAA and therefore is preempted because it applies *only* for the narrow class of terms or agreements relating to the procedures available to claimants in arbitration, and *only* to certain entities whose business may generate small dollar consumer claims.

The enforceability of an arbitration agreement does not and cannot depend on the value of the claims sought to be arbitrated. To subject arbitration agreements to such an *ad hoc* standard for enforceability, which is not generally applicable to other types of contracts, violates the FAA. *See Martindale v. Sandvik, Inc.*, 173 N.J. 76, 86 (N.J. 2002) (quoting *Ferry v. Thomas*, 482 U.S. at 492 n.9 (1987) ("[S]tate law. . . is applicable if that law arose to govern issues concerning the. . . enforceability of contracts generally." However, states may not "decide that a contract is fair enough to enforce all its basic terms . . . but not fair enough to enforce its arbitration clause" because "that kind of policy would place arbitration clauses on an unequal 'footing,' directly contrary to the Act's language and Congress' intent.").

The FAA permits states to enforce or reject arbitration agreements on "grounds as exist at law or in equity for the

revocation of any contract." 9 U.S.C. § 2. The unconscionability rule applied in this case, however, is not a ground that exists for any contract, but rather only for the arbitration agreements that waive class treatment, and only to certain entities whose business may generate claims falling within the newly created subcategory of cases that the New Jersey Supreme Court ambiguously named "low value consumer claims."

This arbitrary line between "low value" and "high value" loans will prove unworkable in practice, because it necessarily would invite courts to draw *post hoc*, arbitrary lines between claims that are substantial "enough" to merit individual arbitration and claims that are thought to be too small to justify it, and without knowing the size of claims to be asserted by other members of the putative class. Compare, *Muhammad* with *Delta Funding*; *see Allied-Bruce Terminix Cos. v. Dobson*, 513 U.S. 265, 282 (1995) (O'Connor, J., concurring) (emphasizing that courts should avoid interpreting FAA in a way that would "foster pre-arbitration litigation that would frustrate the very purpose of the statute"). If this line should be drawn, Congress is in the best position to draw it.

C. The Court Should Grant Certiorari To Resolve The Question It Previously Raised But Did Not Resolve in *Southland Corp. v. Keating*.

In *Keating v. Superior Court*, 645 P.2d 1192, 1195 (Cal. 1982), the plaintiff franchisees brought a class action against their franchisor alleging numerous state law claims. The trial court granted Southland's motion to compel arbitration of the plaintiffs' claims and ordered that the arbitration proceed as a "class arbitration"—even though the parties' agreement did not specify that a class procedure was available in arbitration. The California Supreme Court

granted review of the question whether the trial court could impose class action procedures on the parties. Advancing the same policy rationales the New Jersey Supreme Court identified in this case, the California Supreme Court concluded that the arbitration could go forward as a class proceeding, if the trial court concluded on remand that "gross unfairness" would otherwise result. *Id.* at 1209. Three dissenting justices observed that "[a]rbitration is a matter of agreement," and that the parties' arbitration contracts "do not provide for class arbitration, nor have the parties subsequently agreed thereto." *Id.* at 1214.

This Court noted probable jurisdiction over the question "whether arbitration under the federal Act is impaired when a class-action structure is imposed on the process by the state courts." *Southland*, 465 U.S. at 3. This Court ultimately dismissed that question for lack of jurisdiction, finding that the class arbitration procedure had been challenged below on state law grounds only. *Id.* at 9.

This case raises the same question left unanswered in *Southland*, with two significant twists. First, the parties' arbitration agreement in *Southland* was silent as to whether class action procedures were available in arbitration. In contrast, County Bank's arbitration agreement with Muhammad ***expressly precluded*** class action procedures. Second, the court determined that this revision was appropriate only in consumer cases likely to generate "low value" claims. Thus, for companies doing business in New Jersey, class waivers are available only if the companies' interaction with consumers does not generate "low value" claims, notwithstanding what the parties' agreement actually provides. Only if the claim is large enough – and "large enough" is to be determined case by case with no guidance – will the parties be permitted to arbitrate their claims as agreed.

The jurisdictional impediments to review in *Southland* do not exist here. The question whether the FAA precludes the state court from writing class procedures into the parties' arbitration agreement was raised below on a motion for reconsideration – the first opportunity to do so.[14]

II. THE NEW JERSEY SUPREME COURT'S RULING DENIES PETITIONERS DUE PROCESS BY RETROACTIVELY ENFORCING A NEW INTERPRETATION OF NEW JERSEY LAW.

In *Muhammad*, the New Jersey Supreme Court articulated a new legal principle and applied it retroactively to the Petitioners, thus violating Petitioners' procedural due process rights. In its Opinion, the New Jersey Supreme Court expressly noted that the issue of class arbitration "specifically has never before been examined by this Court." App. A at 17-18.

New Jersey law prior to *Muhammad* held that a waiver of certain rights in an arbitration clause would be enforced so long as they were sufficiently notorious and specific. *Gras v. Associates First Capital Co.*, 346 N.J. Super. 42, 49-57 (App. Div. 2001), *cert. denied*, 171 N.J. 445 (2002). As shown above, pp. 8-9, the provisions here were both specific and notorious. In *Muhammad*, the Court created a new rule that distinguished between "low value" and "high value" claims in determining that a class arbitration waiver is unconscionable and unenforceable when it involves an undefined small amount of money. Meanwhile, a separate ruling on the same day in *Delta Funding*, *supra*, held that such waivers *were* enforceable and not unconscionable when

[14] Prior to the New Jersey Supreme Court's ruling, the lower trial courts had ruled in compliance with the FAA, and no preemption question existed.

they involved a larger monetary claim. App D at 10. Prior to *Muhammad* and *Delta Funding*, New Jersey law did not differentiate between "low value" and "high value" claims.

If applied at all, the new distinction cannot be applied retroactively to the parties here because to do so would cause manifest injustice. "Retroactivity is not favored in the law." *Bowen v. Georgetown Univ. Hospital*, 488 U.S. 204, 208 (1988), *see* H. Broom, Legal Maxims 24 (8th ed. 1911) ("Retrospective laws are, as a rule, of questionable policy, and contrary to the general principle that legislation by which the conduct of mankind is to be regulated ought to deal with future acts, and ought not to change the character of past transactions carried on upon the faith of the then existing law"). Federal law establishes that there are explicit and implied limitations on the legislature's power to impose laws retroactively. Article I, Section 10 of the U.S. Constitution provides that "[n]o State shall. . . pass any. . . law impairing the obligation of contracts." Just as legislatures are barred, so are the courts. All statutes with retroactive elements are subject to scrutiny under the due process clause of the Fourteenth Amendment of the U.S. Constitution. U.S. Const. amend. XIV, § 1.

A court may not automatically apply a change in the law retroactively where the application of that law attaches new legal consequences to completed, past conduct that was legal at the time. *Usery v. Turner Elkhorn Mining Co.*, 428 U.S. 1, 15-16 (1976). If a decision establishes a new principle of law by overruling past precedent or by deciding an issue of first impression, it should be applied only prospectively. *Coons v. American Honda Motor Co.*, 96 N.J. 419, 427, 476 A.2d 763 (1984), cert. denied, 469 U.S. 1123, 105 S.Ct. 808, 83 L.Ed.2d 800 (1985).

If allowed to stand, the Court's ruling in *Muhammad* will effectively invalidate thousands of existing contracts in

which the parties expressly waived certain rights to court proceedings and class actions. The decision also impacts every lender and merchant offering credit cards to New Jersey residents on the basis of the protection provided by the previous law and their legally valid agreements. Retail sales companies and basic service providers are laid open to massive unplanned litigation risk. Such a sweeping application of a fact-specific analysis is arbitrary and irrational and cannot be the basis for retroactive application. *Usery*, *supra*, 428 U.S. at 15.

The ruling in *Muhammad* goes far beyond imposing additional, unnegotiated obligations on Petitioners. It imposes terms that directly contradict the express agreement of the parties. A retrospective application of the ruling in *Muhammad* will result in lengthy and expensive litigation that was not anticipated by either party at the time of entering into the contract, and it will have the chilling effect of discouraging other businesses from lending in this so-called "low value" arena, an area in which customers arguably need additional options, not fewer.

III. THE RULING BELOW UNDULY BURDENS INTERSTATE COMMERCE BY SEEKING TO IMPOSE DISPARATE REQUIREMENTS ON ARBITRATION AGREEMENTS MADE IN THE INTERSTATE MARKET.

Section 2 of the FAA declares pre-dispute arbitration agreements "valid, irrevocable, and enforceable" because "arbitration saves time, saves trouble, saves money." Joint Hearings on S. 1005 and H.R. 646 Before the Subcomms. of the Comms. on the Judiciary, 68th Cong., 1st Sess. 7 (1924) (statement of Charles Bernheimer, N.Y. Chamber of Commerce); *see also* H.R. Rep. No. 68-96, at 2 (1924) ("the costliness and delays of litigation. . .can be largely eliminated by agreements for arbitration, if arbitration

agreements are made valid and enforceable"). As Congress later explained, arbitration usually is "cheaper and faster than litigation," has "simpler procedural and evidentiary rules," "minimizes hostility," and is "more flexible in regard to scheduling." H.R. REP. No. 97-542, at 13 (1982). This Court, too, has recognized the superior "simplicity, informality, and expedition of arbitration." *Mitsubishi Motors Corp. v. Soler ChryslerPlymouth, Inc.*, 473 U.S. 614, 628 (1985); *see also Dean Witter*, 470 U.S. at 221 (recognizing that twin goals of FAA are "enforcement of private agreements [to arbitrate] and encouragement of efficient and speedy dispute resolution").

Class-action procedures, by contrast, severely hinder the low-cost and efficient resolution of disputes that is the hallmark of arbitration. Class actions first require a lengthy class certification proceeding. If, after extensive discovery and hearings, a class is certified, there must be full and adequate notice to class members and an opportunity to opt out. Discovery commensurate with the now-increased stakes of the litigation begins next and often continues for years. If the defendant settles to curtail increasing costs, another round of notice followed by a fairness hearing, complete with extensive briefing by both sides and by any objectors then follows. If the defendant chooses not to settle, a class-wide trial follows - one in which the parties must present the common and individualized elements of their claims and defenses.

Forcing Petitioners to defend against the time-consuming and expensive class action procedures over a previously negotiated waiver of those proceedings eliminates the distinction between arbitration and litigation, but also presents businesses with an impossible scenario. While class arbitration would increase the stakes exponentially over an individual arbitration, any classwide arbitral award would remain reviewable only for fraud, corruption or bias, see 9

U.S.C. § 10, or "manifest disregard" of the law, see *Wilko v. Swan*, 346 U.S. 427, 436-437 (1953), overruled on other grounds by *Rodriguez de Quijas v. Shearson/Am. Express, Inc.*, 490 U.S. 477 (1989).

This standard of review often will be insufficient to avoid an erroneous, yet potentially massive, class-wide judgment. Precluding class waivers also is contrary to the goals of the arbitration process – to provide an efficient and cost effective way to resolve disputes. As Justice Thomas has explained, a rule that "discourages the use of arbitration agreements" is "completely inconsistent with the policies underlying the FAA." *EEOC v. Waffle House, Inc.*, 534 U.S. 279, 310 (2002) (Thomas, J., dissenting); *see also Iberia Credit Bureau, Inc. v. Cingular Wireless LLC*, 379 F.3d 159, 175-176 (5th Cir. 2004) (for parties to demand "all of the procedural accoutrements that accompany a judicial proceeding" would undermine "the point of arbitration").

By eliminating the class waiver from thousands of County Bank contracts, New Jersey's rule disproportionately burdens arbitration and hence violates the Commerce Clause. *Cf. Best & Co. v. Maxwell*, 311 U.S. 454, 455 (1940) ("The commerce clause forbids discrimination, whether forthright or ingenious."). Should the current conflict in the law persist, the enforceability of form contracts containing arbitration provisions will vary from state to state based on the *ad hoc* policy judgments of the various states' courts as to whether the arbitration provision (or some feature of it) shocks the conscience. In fact, as demonstrated here, enforceability of the same form contract could differ in different cases within the same state, should the state choose to draw additional lines between types of claims (as here), or types of consumers, or types of services.

The uncertainty created by New Jersey's *ad hoc*, state specific approach is a burden not just on arbitration, but also

on interstate commerce. *See BMW of North America, Inc. v. Gore*, 517 U.S. 559, 570-571 ("[O]ne state's power to impose burdens on the interstate market [through a state court's actions in a civil case]. . .is not only subordinate to the federal power over interstate commerce, but is also constrained by the need to respect the interests of other states.") (internal citations omitted). This Court has long stated that the Constitution is equally concerned with state regulation and Congressional regulation of interstate commerce, *see Healy v. Beer Institute*, 491 U.S. 324, 335-336 (1989), but that state regulation attempting to upset that balance must give way to the FAA. *See Southland*, 465 U.S. at 15 ("We are unwilling to attribute to Congress the intent, in drawing on the comprehensive powers of the Commerce Clause, to create a right to enforce an arbitration contract and yet make the right dependent for its enforcement on the particular forum in which it is asserted.").

The New Jersey rule disproportionately burdens arbitration and interstate commerce and must not be allowed to stand. Only Congress, not individual states, has the power to do so.

CONCLUSION

State and federal courts have been seeking resolution to the arbitration questions presented in *Muhammad* for 20 years since this Court raised the preemption question in *Southland*. Certiorari should now be granted and the decision of the New Jersey Supreme Court should be reversed so that the multi-level conflicts, *ad hoc* adjudication, and upheaval in interstate commerce may end, allowing arbitration to move forward as Congress originally intended.

Respectfully submitted,

By: /s/

Claudia T. Callaway – *counsel of record*
Michael M. Berger
Sabrina M. Rose-Smith
Manatt, Phelps & Phillips, LLP
700 12th Street N.W., Suite 1100
Washington, D.C. 20005

Counsel for Main Street Service Corp.

By: /s/

Marc J. Zucker
Susan Verbonitz
Weir & Partners LLP
Suite 500
The Widener Building
1339 Chestnut Street
Philadelphia, PA 19107

Counsel for County Bank of Rehoboth Beach, Delaware

APPENDIX A

Muhammad v. County Bank of Rehoboth Beach, DelawareN.J.,2006.--- A.2d ----Only the Westlaw citation is currently available.

Supreme Court of New Jersey.

Jaliyah MUHAMMAD, on her own behalf and all others similarly situated, Plaintiff-Appellant,

v.

COUNTY BANK OF REHOBOTH BEACH, DELAWARE and Main Street Service Corporation, Defendants-Respondents,

andEasycash, Telecash, John Doe and John Roe, Defendants.

Argued Feb. 14, 2006.

Decided Aug. 9, 2006.

SYNOPSIS

Background: Borrower brought class action against lender and servicer of payday loan, alleging that all defendants violated the New Jersey Consumer Fraud Act, the servicer violated usury law and the New Jersey Racketeer Influenced and Corrupt Organizations Act (RICO), and the lender conspired to violate RICO. Defendants moved to compel arbitration. The Superior Court, Law Division, Union County, granted motion. Borrower appealed, and the Superior Court, Appellate Division, affirmed, 379 N.J.Super. 222, 877 A.2d 340. Borrower appealed.

Holdings: The Supreme Court, LaVecchia, J., held that:

(1) court, rather than arbitrator, was required to determine whether class-action arbitration waiver in loan agreement was valid;

(2) challenge was not a challenge to the contract as a whole but rather was a specific challenge to the arbitration agreement;

(3) as a matter of first impression, class-arbitration waiver contained in arbitration agreement was unconscionable due to public interest at stake; and

(4) class-arbitration waivers were severable such that remainder of the arbitration agreements were enforceable.

Reversed and remanded.

Rivera-Soto, J., concurred in part and dissented in part with opinion.

[1] Alternative Dispute Resolution 25T 134(6)

25T Alternative Dispute Resolution
25TII Arbitration
25TII(B) Agreements to Arbitrate
25Tk131 Requisites and Validity
25Tk134 Validity
25Tk134(6) k. Unconscionability.
Most Cited Cases
The Federal Arbitration Act (FAA) does not preclude an examination into whether the arbitration agreement at issue is unconscionable under state law. 9 U.S.C.A. § § 1 et seq.

[2] Alternative Dispute Resolution 25T 134(3)

25T Alternative Dispute Resolution
25TII Arbitration
25TII(B) Agreements to Arbitrate
25Tk131 Requisites and Validity
25Tk134 Validity
25Tk134(3) k. Validity of Assent.

Most Cited Cases

Alternative Dispute Resolution 25T ⚿134(6)

25T Alternative Dispute Resolution
25TII Arbitration
25TII(B) Agreements to Arbitrate
25Tk131 Requisites and Validity
25Tk134 Validity
25Tk134(6) k. Unconscionability. Most Cited Cases
Generally applicable contract defenses, such as fraud, duress, or unconscionability, may be applied to invalidate arbitration agreements without contravening the Federal Arbitration Act (FAA). 9 U.S.C.A. § 2.

[3] Alternative Dispute Resolution 25T ⚿199

25T Alternative Dispute Resolution

25TII Arbitration
25TII(D) Performance, Breach, Enforcement, and Contest
25Tk197 Matters to Be Determined by Court
25Tk199 k. Existence and Validity of Agreement. Most Cited Cases
The issue of whether the parties have a valid arbitration agreement at all is a gateway question that requires judicial resolution.

[4] Alternative Dispute Resolution 25T ⚿202

25T Alternative Dispute Resolution
25TII Arbitration
25TII(D) Performance, Breach, Enforcement, and Contest
25Tk197 Matters to Be Determined by Court

25Tk202 k. Waiver, Laches, or Estoppel.
Most Cited Cases
Court, rather than arbitrator, was required to determine whether class-action arbitration waiver in loan agreement was valid, as agreement was not silent or even ambiguous as to the availability of class arbitration.

[5] Alternative Dispute Resolution 25T 199

25T Alternative Dispute Resolution
25TII Arbitration
25TII(D) Performance, Breach, Enforcement, and Contest
25Tk197 Matters to Be Determined by Court
25Tk199 k. Existence and Validity of Agreement. Most Cited Cases
A court must decide whether an agreement to arbitrate is valid.

[6] Alternative Dispute Resolution 25T 202

25T Alternative Dispute Resolution
25TII Arbitration
25TII(D) Performance, Breach, Enforcement, and Contest
25Tk197 Matters to Be Determined by Court
25Tk202 k. Waiver, Laches, or Estoppel. Most Cited Cases
Borrower's challenge to class-action arbitration waiver in loan agreement was not a challenge to the contract as a whole, but rather was a specific challenge to the arbitration agreement such that court, rather than arbitrator, could decide validity of waiver; based on their location and subject matter, distinct class-arbitration waivers within arbitration clauses of both loan note and disclosure form and the loan application were part of the arbitration agreements, and not part of the contracts as a whole.

[7] Contracts 95 ⚿1

95 Contracts
95I Requisites and Validity
95I(A) Nature and Essentials in General
95k1 k. Nature and Grounds of Contractual Obligation. Most Cited Cases
Courts may refuse to enforce contracts that are unconscionable.

[8] Contracts 95 ⚿1

95 Contracts
95I Requisites and Validity
95I(A) Nature and Essentials in General
95k1 k. Nature and Grounds of Contractual Obligation. Most Cited Cases
The determination that a contract is one of adhesion is the beginning, not the end, of the inquiry into whether a contract, or any specific term therein, should be deemed unenforceable based on policy considerations.

[9] Contracts 95 ⚿1

95 Contracts
95I Requisites and Validity
95I(A) Nature and Essentials in General
95k1 k. Nature and Grounds of Contractual Obligation. Most Cited Cases
A sharpened inquiry concerning unconscionability is necessary when a contract of adhesion is involved.

[10] Parties 287 ⚿35.1

287 Parties
287III Representative and Class Actions
287III(A) In General

287k35.1 k. In General. Most Cited Cases
The class-action mechanism is valuable to litigants, to the courts, and to the public interest.

[11] Alternative Dispute Resolution 25T 134(6)

25T Alternative Dispute Resolution
25TII Arbitration
25TII(B) Agreements to Arbitrate
25Tk131 Requisites and Validity
25Tk134 Validity
25Tk134(6) k. Unconscionability. Most Cited Cases

Contracts 95 1

95 Contracts
95I Requisites and Validity
95I(A) Nature and Essentials in General
95k1 k. Nature and Grounds of Contractual Obligation. Most Cited Cases
Class-arbitration waiver contained in arbitration agreement in payday loan adhesion contract was unconscionable due to public interest at stake, as class-arbitration bar effectively prevented borrower from pursuing her consumer protection rights and shielded lenders from compliance with state law; action involving complicated financial arrangements and multiple out-of-state entities, and damages amount sought by borrower added up to maximum of less $600. N.J.S.A. 31:1-1, 56:8-2.

Class-arbitration waiver contained in arbitration agreement in payday loan adhesion contract was unconscionable due to public interest at stake, as class-arbitration bar effectively prevented borrower from pursuing her consumer protection rights and shielded lenders from compliance with state law; action involving complicated financial arrangements and

multiple out-of-state entities. and damages amount sought by borrower added up to maximum of less $600. N.J.S.A. 31:1-1. 56:8-2.

[12] Contracts 95 ⚿1

95 Contracts
95I Requisites and Validity
95I(A) Nature and Essentials in General
95k1 k. Nature and Grounds of Contractual Obligation. Most Cited Cases
Adhesive consumer contracts which are ordinarily enforceable nonetheless may rise to the level of unconscionability when substantive contractual terms and conditions impact public interests adversely.

[13] Contracts 95 ⚿114

95 Contracts
95I Requisites and Validity
95I(F) Legality of Object and of Consideration
95k114 k. Exemption from Liability. Most Cited Cases

Exculpatory waivers that seek a release from a statutorily imposed duty are void as against public policy.

[14] Contracts 95 ⚿1

95 Contracts
95I Requisites and Validity
95I(A) Nature and Essentials in General
95k1 k. Nature and Grounds of Contractual Obligation. Most Cited Cases
Class-action waivers are problematic when the waiver is found in a consumer contract of adhesion in a setting in which disputes between the contracting parties predictably

involve small amounts of damages.

[15] Contracts 95 🔑1

95 Contracts
95I Requisites and Validity
95I(A) Nature and Essentials in General
95k1 k. Nature and Grounds of Contractual Obligation. Most Cited Cases
When substantial damages are at stake, the court considering the validity of a class-action waiver in a contract of adhesion should consider whether the availability of attorney's fees, including any possible fee enhancement, in conjunction with a substantial potential damages award, including any potential statutory multipliers, would allow a substantial number of consumers to obtain counsel and seek relief such that the waiver would be valid.

[16] Alternative Dispute Resolution 25T 🔑111

25T Alternative Dispute Resolution
25TII Arbitration
25TII(A) Nature and Form of Proceeding
25Tk111 k. Nature, Purpose, and Right to Arbitration in General. Most Cited Cases
The purpose of arbitration is not to discourage consumers from seeking vindication of their rights.

[17] Alternative Dispute Resolution 25T 🔑140

25T Alternative Dispute Resolution
25TII Arbitration
25TII(B) Agreements to Arbitrate
25Tk140 k. Severability. Most Cited Cases
Unconscionable class-arbitration waivers in arbitration agreements contained in payday loan adhesion contracts were severable such that remainder of the arbitration

agreements were enforceable, as use of language "to the extent permitted by law" in broad class-action waivers indicated intention that arbitration agreement would be implemented whether and to whatever extent class-wide arbitration might be barred.

[18] Alternative Dispute Resolution 25T 140

25T Alternative Dispute Resolution
25TII Arbitration
25TII(B) Agreements to Arbitrate
25Tk140 k. Severability. Most Cited Cases
If all the provisions of the arbitration clause are enforceable, then the court must compel arbitration according to the terms of the agreement; if, however, some or all of its provisions are not enforceable, then the court must determine whether the unenforceable provisions are severable.

[19] Alternative Dispute Resolution 25T 140

25T Alternative Dispute Resolution
25TII Arbitration
25TII(B) Agreements to Arbitrate
25Tk140 k. Severability. Most Cited Cases
Severability of unenforceable portions of an arbitration agreement is decided as a matter of state law.

[20] Alternative Dispute Resolution 25T 140

25T Alternative Dispute Resolution
25TII Arbitration
25TII(B) Agreements to Arbitrate
25Tk140 k. Severability. Most Cited Cases
If the offensive terms of an arbitration agreement are severable, then the court must compel arbitration according to the remaining, valid terms of the parties' agreement; the court should deny a motion to compel arbitration only where

the invalid terms of the arbitration clause render the entire clause void as a matter of state law.

On appeal from Superior Court, Appellate Division, whose opinion is reported at 379 N.J.Super. 222, 877 A.2d 340 (2005).

Michael J. Quirk, a member of the New York and District of Columbia bars, argued the cause for appellant (Trujillo, Rodriguez & Richards and Williams, Cuker & Berezofsky, attorneys; Mr. Quirk, Donna Siegel Moffa and Mark R. Cuker, on the briefs).

Marc J. Zucker and Claudia T. Callaway, a member of the District of Columbia bar, argued the cause for respondents (Weir & Partners, attorneys for County Bank of Rehoboth Beach, Delaware and Sweeney & Sheehan, attorneys for Main Street Service Corporation; Mr. Zucker, Ms. Callaway, Susan M. Verbonitz, John Michael Kunsch, on the briefs).
David G. McMillin argued the cause for amicus curiae Legal Services of New Jersey (Melville D. Miller, Jr., President, attorney; Mr. McMillin, Mr. Miller and Christopher Hill, on the brief).
Jeffrey C. Burstein, Assistant Attorney General, argued the cause for amici curiae Attorney General of New Jersey and The New Jersey Division of Consumer Affairs (Zulima V. Farber, Attorney General, attorney; Mr. Burstein and Carol G. Jacobson, Deputy Attorney General, on the brief).
David M. Gossett, a member of the Illinois and District of Columbia bars, argued the cause for amicus curiae Chamber of Commerce of the United States of America (Drinker Biddle & Reath, attorneys; Mr. Gossett, Evan M. Tager, a member of the New York and District of Columbia bars, Robin S. Conrad, a member of the District of Columbia bar, Amar D. Sarwal, a member of the District of Columbia bar, of counsel; Andrew B. Joseph, on the brief).

William J. Pinilis submitted a brief on behalf of amici curiae AARP, Consumers League of New Jersey and National Association of Consumer Advocates.

Marvin J. Brauth and Jeffrey J. Brookner submitted a brief on behalf of amicus curiae New Jersey Business and Industry Association (Wilentz, Goldman & Spitzer, attorneys; Mr. Brauth, of counsel; Mr. Brauth and Mr. Brookner, on the brief).*Michael J. Quirk,* a member of the New York and District of Columbia bars, argued the cause for appellant (*Trujillo, Rodriguez & Richards* and *Williams, Cuker & Berezofsky,* attorneys; *Mr. Quirk, Donna Siegel Moffa* and *Mark R. Cuker,* on the briefs).*Marc J. Zucker* and *Claudia T. Callaway,* a member of the District of Columbia bar, argued the cause for respondents (*Weir & Partners,* attorneys for County Bank of Rehoboth Beach, Delaware and *Sweeney & Sheehan,* attorneys for Main Street Service Corporation; *Mr. Zucker, Ms. Callaway, Susan M. Verbonitz, John Michael Kunsch,* on the briefs).*David G. McMillin* argued the cause for amicus curiae Legal Services of New Jersey (*Melville D. Miller, Jr.,* President, attorney; *Mr. McMillin, Mr. Miller* and *Christopher Hill,* on the brief).*Jeffrey C. Burstein,* Assistant Attorney General, argued the cause for amici curiae Attorney General of New Jersey and The New Jersey Division of Consumer Affairs (*Zulima V. Farber,* Attorney General, attorney; *Mr. Burstein* and *Carol G. Jacobson,* Deputy Attorney General, on the brief).*David M. Gossett,* a member of the Illinois and District of Columbia bars, argued the cause for amicus curiae Chamber of Commerce of the United States of America (*Drinker Biddle & Reath,* attorneys; *Mr. Gossett, Evan M. Tager,* a member of the New York and District of Columbia bars, *Robin S. Conrad,* a member of the District of Columbia bar, *Amar D. Sarwal,* a member of the District of Columbia bar, of counsel; *Andrew B. Joseph,* on the brief).*William J. Pinilis* submitted a brief on behalf of amici curiae AARP, Consumers League of New Jersey and National Association of Consumer Advocates.*Marvin J. Brauth* and *Jeffrey J. Brookner* submitted a brief on behalf of

amicus curiae New Jersey Business and Industry Association (*Wilentz, Goldman & Spitzer,* attorneys; *Mr. Brauth,* of counsel; *Mr. Brauth and Mr. Brookner,* on the brief).

Justice LaVECCHIA delivered the opinion of the Court.

*1 In this appeal we must determine whether a provision in an arbitration agreement that is part of a consumer contract of adhesion is unconscionable and therefore unenforceable because it forbids class-wide arbitration. Plaintiff entered into a short-term loan agreement, the terms of which she claims violate the State's consumer-fraud statutes. Her complaint includes allegations that the State's civil usury limits are being evaded in loan transactions such as hers by means of a conspiracy involving complex financial dealings among out-of-state financial entities. The damages allegedly caused by such transactions are small on an individual-by-individual basis, but are substantial when aggregated into a class claim. Plaintiff seeks, therefore, to pursue a class action and is willing to pursue her class-wide claim in the arbitral forum but for the arbitration agreement's class-arbitration bar. Both the trial court and the Appellate Division found the class-arbitration bar enforceable.

Applying the controlling test for determining unconscionability for contracts of adhesion set forth in *Rudbart v. North Jersey District Water Supply Commission,* 127 *N.J.* 344, 605 *A.*2d 681, *cert. denied,* 506 *U.S.* 871, 113 *S.Ct.* 203, 121 *L. Ed.*2d 145 (1992), we hold that the class-arbitration waiver in this consumer contract is unenforceable. Such a waiver would be unconscionable whether applied in a lawsuit or in arbitration. We further conclude that the appropriate remedy in these circumstances is to sever the unconscionable provision and enforce the otherwise valid arbitration agreement.

I.

Defendant County Bank of Rehoboth Beach, Delaware (County Bank) is a federally-insured depository institution chartered under Delaware law. Defendant Main Street Service Corp. (Main Street) is a loan servicer for County Bank. Main Street operates a telephone service center in Pennsylvania. Defendants Easy Cash and Telecash are registered trade names of County Bank.

On May 23, 2003, plaintiff Jaliyah Muhammad, a part-time student at Berkeley College in Paramus, received a short-term, single advance, unsecured loan of $200 from County Bank. According to the terms of the LOAN NOTE AND DISCLOSURE form that Muhammad signed, the principal, along with a finance charge of sixty dollars, was due on June 13, 2003. The annual percentage rate listed on the loan note was 608.33%. According to Muhammad, she twice extended the loan (with a sixty dollar finance charge each time) because she could not repay it, resulting in a total of $180 in finance charges. Those facts are unchallenged by defendants. Muhammad also obtained two similar loans from County Bank, dated April 28, 2003 and June 6, 2003.

Muhammad had to complete and return three pages of standard form contracts in order to receive a loan. The first two pages, entitled "LOAN APPLICATION," were signed by Muhammad on April 28, 2003. Muhammad did not have to complete that form again in connection with the loans made on May 23, 2003 and June 6, 2003. The first page of the LOAN APPLICATION requested general personal information. The second page contained the relevant provisions concerning arbitration:

*2 AGREEMENT TO ARBITRATE ALL DISPUTES: By signing below and to induce us, County Bank of Rehoboth Beach, Delaware, to process your application for a loan, you and we agree that any and all claims, disputes or

controversies that we or our servicers or agents have against you or that you have against us, our servicers, agents, directors, officers and employees, that arise out of your application for a loan, the Loan Note or Agreement that you must sign to obtain the loan, this agreement to arbitrate all disputes, collection of the loan, or alleging fraud or misrepresentation, whether under the common law or pursuant to federal or state statute or regulation, including the matters subject to arbitration, *or otherwise, shall be resolved by binding individual (and not class) arbitration* by and under the Code of Procedures of the National Arbitration Forum ("NAF") in effect at the time the claim is filed. This agreement to arbitrate all disputes shall apply no matter by whom or against whom the claim is filed....

NOTICE: YOU AND WE WOULD HAVE HAD A RIGHT OR OPPORTUNITY TO LITIGATE DISPUTES THROUGH A COURT AND HAVE A JUDGE OR JURY DECIDE THE DISPUTES BUT HAVE AGREED INSTEAD TO RESOLVE DISPUTES THROUGH BINDING ARBITRATION.

AGREEMENT NOT TO BRING, JOIN OR PARTICIPATE IN CLASS ACTIONS: To the extent permitted by law, by signing below you agree that you will not bring, join or participate in any class action as to any claim, dispute or controversy you may have against us or our agents, servicers, directors, officers and employees. You agree to the entry of injunctive relief to stop such a lawsuit or to remove you as a participant in the suit. You agree to pay the costs we incur, including our court costs and attorney's fees, in seeking such relief. This agreement is not a waiver of any of your rights and remedies to pursue a claim individually and not as a class action in binding arbitration as provided above. This agreement not to bring or participate in class action suits is an independent agreement and shall survive the closing and repayment of the loan for which you are applying.

[(Emphasis added).]

Above the signature line, the LOAN APPLICATION also stated that "[b]y signing below you also agree to the Agreement to Arbitrate All Disputes and the Agreement Not To Bring, Join or Participate In Class Actions...."

In respect of the May 23, 2003 loan, Muhammad also executed a LOAN NOTE AND DISCLOSURE form that included the following language.

AGREEMENT TO ARBITRATE ALL DISPUTES: You and we agree that any and all claims, disputes or controversies between you and us and/or the Company, any claim by either of us against the other or the Company (or the employees, officers, directors, agents or assigns of the other or the Company) and any claim arising from or relating to your application for this loan or any other loan you previously, now or may later obtain from us, this Loan Note, this agreement to arbitrate all disputes, your agreement not to bring, join or participate in class actions, regarding collection of the loan, alleging fraud or misrepresentation, whether under the common law or pursuant to federal, state or local statutes, regulation or ordinance, including disputes as to the matters subject to arbitration, or otherwise, *shall be resolved by binding individual (and not joint) arbitration* by and under the Code of Procedure of the National Arbitration Forum ("NAF") in effect at the time the claim is filed. This agreement to arbitrate all disputes shall apply no matter by whom or against whom the claim is filed.... This arbitration agreement is made pursuant to a transaction involving interstate commerce. It shall be governed by the Federal Arbitration Act, 9 U.S.C. Sections 1-16....

***3** NOTICE: YOU AND WE WOULD HAVE HAD A RIGHT OR OPPORTUNITY TO LITIGATE DISPUTES THROUGH A COURT AND HAVE A JUDGE OR JURY DECIDE THE DISPUTES BUT HAVE AGREED INSTEAD TO RESOLVE DISPUTES THROUGH BINDING ARBITRATION.

AGREEMENT NOT TO BRING, JOIN OR PARTICIPATE

IN CLASS ACTIONS: To the extent permitted by law, you agree that you will not bring, join or participate in any class action as to any claim, dispute or controversy you may have against us, our employees, officers, directors, servicers and assigns. You agree to the entry of injunctive relief to stop such a lawsuit or to remove you as a participant in the suit. You agree to pay the attorney's fees and court costs we incur in seeking such relief. This Agreement does not constitute a waiver of any of your rights and remedies to pursue a claim individually and not as a class action in binding arbitration as provided above.
[(Emphasis added).]

If that were not clear enough, directly above the signature line, the LOAN NOTE AND DISCLOSURE form also stated, that "BY SIGNING BELOW, YOU AGREE TO ALL OF THE TERMS OF THIS NOTE, INCLUDING THE AGREEMENT TO ARBITRATE ALL DISPUTES AND THE AGREEMENT NOT TO BRING, JOIN OR PARTICIPATE IN CLASS ACTIONS."

Thus, the contracts signed by Muhammad contain two types of class-action prohibitions. The first, referred to herein as the "class-arbitration waivers," are found within the text of the arbitration clauses and highlighted above. They specifically bar class claims in arbitration. The second, referred to herein as the "broad class-action waivers," are separate from the arbitration clauses and prohibit Muhammad from bringing or participating in class-action suits brought in court as well as class claims brought in arbitration.

In February 2004, Muhammad filed a putative class-action suit in New Jersey Superior Court against County Bank, Easy Cash, Telecash, Main Street, John Doe, and John Roe. The complaint alleged that Easy Cash, Telecash, and Main Street violated the Consumer Fraud Act (CFA), *N.J.S.A.*

56:8-2, the civil usury statute, *N.J.S.A.* 31:1-1, and the New Jersey RICO statute, *N.J.S.A.* 2C:41-1, by charging, and conspiring to charge, illegal rates of interest. The complaint further alleged that County Bank aided and abetted the unlawful conduct of the other defendants by renting out its name and status without actually funding or meaningfully participating in the loans. Muhammad requested injunctive relief, restitution, damages, penalties, and costs.

Defendants removed the action to federal district court, but because Muhammad's claims were determined by that court not to be preempted by the Depository Institutions Deregulation and Monetary Control Act of 1980, 12 *U.S.C.* § 1831d, the case was remanded to state court. Defendants thereupon filed a motion to compel arbitration and to stay the action pending arbitration. They also filed a motion requesting a protective order in respect of discovery. Muhammad opposed defendants' motions and filed a cross-motion concerning discovery. Muhammad argued that the arbitration agreement was unconscionable based on the class-action waiver, discovery limitations in NAF's rules, the costs of the arbitration, and the bias inherent in NAF as an arbitration forum.[FN1] In response, defendants offered to arbitrate Muhammad's claims in the American Arbitration Association rather than the NAF-an offer that Muhammad rejected.

***4** The trial court granted defendants' motion to compel arbitration pursuant to the Federal Arbitration Act (FAA), 9 *U.S.C.* § 4, and stayed the case pending arbitration. Muhammad filed a motion for leave to appeal, which was granted. In a published decision, the Appellate Division affirmed the trial court. *Muhammad v. County Bank of Rehoboth Beach*, 379 *N.J.Super.* 222, 877 *A.*2d 340 (App.Div.2005). Applying *Rudbart, supra*, 127 *N.J.* at 353, 605 *A.*2d 681, the panel concluded that the arbitration agreement was not unconscionable. *Muhammad, supra*, 379

N.J.Super. at 237-48, 877 *A.*2d 340. In upholding the class-arbitration bar specifically, the Appellate Division relied on its earlier decision in *Gras v. Associates First Capital Corp.*, 346 *N.J.Super.* 42, 786 *A.*2d 886 (2001), *certif. denied*, 171 *N.J.* 445, 794 *A.*2d 184 (2002), which, the panel believed, "directly address[ed]" the class-action waiver issue. *Muhammad, supra*, 379 *N.J.Super.* at 244-48, 877 *A.*2d 340. Judge Kestin filed a separate concurring opinion. *Id.* at 249, 877 A.2d 340.

Plaintiff filed a motion for leave to appeal, which we granted. 185 *N.J.* 254 (2005). Legal Services of New Jersey filed a brief as amicus curiae in support of Muhammad. AARP, the Consumers League of New Jersey, and the National Association of Consumer Advocates filed a joint brief in support of Muhammad. Also, the Attorney General on behalf of the New Jersey Division of Consumer Affairs filed a brief in Muhammad's support. The Chamber of Commerce of the United States of America and the New Jersey Business and Industry Association filed amicus briefs in support of defendants.

II.

A.

[1] Congress enacted the FAA, 9 *U.S.C.* § § 1-16, "to abrogate the then-existing common law rule disfavoring arbitration agreements 'and to place arbitration agreements upon the same footing as other contracts.' " *Martindale v. Sandvik, Inc.*, 173 *N.J.* 76, 84, 800 *A.*2d 872 (2002) (quoting *Gilmer v. Interstate/Johnson Lane Corp.*, 500 *U.S.* 20, 24, 111 *S.Ct.* 1647, 1651, 114 *L. Ed.*2d 26, 36 (1991)). Section 2 of the FAA provides that arbitration agreements covered by the Act "shall be valid, irrevocable, and enforceable save

upon grounds as exist at law or in equity for the revocation of any contract." 9 *U.S.C.* § 2. "In enacting section 2 of the FAA, 'Congress declared a national policy favoring arbitration and withdrew the power of the states to require a judicial forum for the resolution of claims which the contracting parties agreed to resolve by arbitration.' " *Martindale, supra,* 173 *N.J.* at 84, 800 *A.*2d 872 (quoting *Southland Corp. v. Keating,* 465 *U.S.* 1, 10, 104 *S.Ct.* 852, 858, 79 *L. Ed.*2d 1, 12 (1984)). The FAA, however, does not preclude an examination into whether the arbitration agreement at issue is unconscionable under state law. *Id.* at 85-86, 800 A.2d 872.

[2][3] "[G]enerally applicable contract defenses, such as fraud, duress, or *unconscionability,* may be applied to invalidate arbitration agreements without contravening § 2." *Doctor's Assocs. ., Inc. v. Casarotto,* 517 *U.S.* 681, 687, 116 *S.Ct.* 1652, 1656, 134 *L. Ed.*2d 902, 909 (1996) (emphasis added); *see also Discover Bank v. Superior Court,* 36 *Cal.*4th 148, 30 *Cal.Rptr.*3d 76, 113 *P.*3d 1100, 1112-13 (Cal.2005) (stating that "the FAA does not federalize the law of unconscionability or related contract defenses except to the extent that it forbids the use of such defenses to discriminate against arbitration clauses."). Furthermore, "whether the parties have a valid arbitration agreement at all" is a "gateway" question that requires judicial resolution. *Green Tree Fin. Corp. v. Bazzle,* 539 *U.S.* 444, 452, 123 *S.Ct.* 2402, 2407, 156 *L. Ed.*2d 414, 422 (2003) (plurality opinion).

***5** [4][5] It is clear that under *Prima Paint Corp. v. Flood & Conklin Manufacturing Co.,* 388 *U.S.* 395, 403-04, 87 *S.Ct.* 1801, 1806, 18 *L. Ed.*2d 1270, 1277 (1967), "a court must decide whether [an] agreement to arbitrate is valid." *Barker v. Golf U.S.A., Inc.,* 154 *F.*3d 788, 791 (8th Cir.1998), *cert. denied,* 525 *U.S.* 1068, 119 *S.Ct.* 796, 142 *L. Ed.*2d 659 (1999). That said, were this contract silent or ambiguous

about the availability of class-wide arbitration, an arbitrator would have to resolve the question of contract interpretation. *See Bazzle, supra,* 539 *U.S.* at 451, 123 *S.Ct.* at 2407, 156 *L. Ed.*2d at 422 (holding that when arbitration agreement is silent on subject, arbitrator is to decide "whether the agreement forbids class arbitration"). The instant agreement is not silent, however, or even ambiguous as to the availability of class arbitration. Not only does the LOAN NOTE AND DISCLOSURE FORM state that all disputes "shall be resolved by binding individual (and not joint) arbitration," but the April 28, 2003 LOAN APPLICATION also states all disputes "shall be resolved by binding individual (and not class) arbitration." Both documents also reference the NAF rules of procedure, which bar class-wide arbitrations unless all parties consent. *See NAF Rule* 19(a). Furthermore, in addition to the class-arbitration waivers found in the arbitration agreements themselves, the broad class-action waivers found elsewhere in the contracts also contain clear and unmistakable language prohibiting Muhammad's use of a class mechanism.

Other courts similarly have distinguished *Bazzle.* For example, in *Gipson v. Cross Country Bank,* 354 *F.Supp.*2d 1278, 1286 (M.D.Ala.2005), the court, in the course of upholding a particular class-arbitration waiver, stated that

> [t]he contract before this court now is distinguishable from the one in *Bazzle,* because here the clause prohibiting class arbitration is clear, that is, there is no issue of contract interpretation as there was in *Bazzle.* Put another way, the Court plurality in *Bazzle* felt that the answer as to whether the contracts allowed or prohibited class arbitration was "not completely obvious," hence contract interpretation, which is the realm of the arbitrator, would be necessary. Here, however, an arbitrator need not interpret the contract's class action waiver clause, because the contract expressly prohibits class arbitration, thereby concerning "the validity of the arbitration clause," which the *Bazzle* plurality

indicated could fall under the narrow exception concerning matters "contracting parties would likely have expected a court" to decide. There is no need for anyone to decide "whether the contract[ ] forbid[s] class arbitration." It expressly and unequivocally does. The only issue is whether such a clear prohibition is valid and enforceable....
[(Citations omitted).]

[6] For completeness we note defendants' argument that Muhammad's claims must fail because her challenge to the class-action waiver should be viewed as a challenge to the contract as a whole, and not as a specific challenge to the arbitration agreement. *Prima Paint, supra,* 388 *U.S.* 395, 87 *S.Ct.* 1801, 18 *L. Ed.*2d 1270, and *Buckeye Check Cashing, Inc. v. Cardegna,* --- *U.S.* ----, 126 *S.Ct.* 1204, 163 *L. Ed.*2d 1038 (2006), hold that because arbitration agreements are, as a matter of federal arbitration law, severable from the remainder of a contract, a challenge to a contract as a whole is for an arbitrator to decide. In this matter, however, there are two types of class-action waivers in the contracts Muhammad signed: the class-arbitration waivers and the broad class-action waivers. The broad class-action waivers could be considered distinct from the arbitration agreement in the contracts, and thus could be considered part of the "contract as a whole." In that circumstance, under *Prima Paint* and *Buckeye,* an arbitrator would address the unconscionability of the broad class-action waivers. That situation is not before us, however, because there are distinct class-arbitration waivers within the arbitration clauses of both the LOAN NOTE AND DISCLOSURE form and the APPLICATION. Those class-arbitration waivers, based on their location and subject matter, are part of the arbitration agreements, and not part of the contracts as a whole. As such, we are empowered to address this challenge.

***6** Because federal arbitration law does not prevent us from examining the validity of the class-arbitration waiver, we

turn then to our own state law requirements in respect of contract unconscionability.[FN2]

B.

[7] It is well settled that courts "may refuse to enforce contracts that are unconscionable." *Saxon Constr. & Management Corp. v. Masterclean of N.C., Inc.*, 273 *N.J.Super.* 231, 236, 641 *A.*2d 1056 (App.Div.), *certif. denied*, 137 *N.J.* 314, 645 *A.*2d 142 (1994); *see also* *N.J.S.A.* 12A:2-302 (adopting Uniform Commercial Code provision recognizing unconscionability as basis for voiding contract or clause therein). The seminal case of *Rudbart, supra,* set out factors for courts to consider when determining whether a specific term in a contract of adhesion is unconscionable and unenforceable. 127 *N.J.* at 356, 605 *A.*2d 681. In *Rudbart, supra,* this Court recognized that adhesion agreements necessarily involve indicia of procedural unconscionability. *Ibid.; see generally* *Sitogum Holdings, Inc. v. Ropes*, 352 *N.J.Super.* 555, 564-66, 800 *A.*2d 915 (Ch.Div.2002) (observing that unconscionability traditionally entails discussion of two factors: procedural unconscionability, which "can include a variety of inadequacies, such as age, literacy, lack of sophistication, hidden or unduly complex contract terms, bargaining tactics, and the particular setting existing during the contract formation process," and substantive unconscionability, which generally involves harsh or unfair one-sided terms). *Rudbart, supra,* notes that "the essential nature of a contract of adhesion is that it is presented on a take-it-or-leave-it basis, commonly in a standardized printed form, without opportunity for the 'adhering' party to negotiate except perhaps on a few particulars." 127 *N.J.* at 353, 605 *A.*2d 681.

[8][9] The determination that a contract is one of adhesion, however, "is the beginning, not the end, of the inquiry" into

whether a contract, or any specific term therein, should be deemed unenforceable based on policy considerations. *Id.* at 354, 605 A.2d 681. A sharpened inquiry concerning unconscionability is necessary when a contract of adhesion is involved.

[I]n determining whether to enforce the terms of a contract of adhesion, courts have looked not only to the take-it-or-leave-it nature or the standardized form of the document but also to [(1)] the subject matter of the contract, [(2)] the parties' relative bargaining positions, [(3)] the degree of economic compulsion motivating the "adhering" party, and [(4)] the public interests affected by the contract.

[*Id.* at 356, 605 A.2d 681.]

Because adhesion contracts invariably evidence some characteristics of procedural unconscionability, the Court required a careful fact-sensitive examination into substantive unconscionability.[FN3] *Ibid. Rudbart's* multi-factor analysis generally conforms to the case-by-case approach widely used for evaluating claims of unconscionability. *See Cheshire Mortg. Serv. v. Montes*, 223 *Conn.* 80, 612 *A.*2d 1130, 1135 (Conn.1992) (stating that, under the UCC, "[t]he determination of unconscionability is to be made on a case-by-case basis, taking into account all of the relevant facts and circumstances.").

C.

*7 The unconscionability issue in this matter centers on access to a class-wide proceeding in the arbitral setting. Although class arbitration specifically has never before been examined by this Court, the merits of the class-action procedure have been acknowledged many times in the context of court litigation. "By permitting claimants to band together, class actions equalize adversaries and provide a

procedure to remedy a wrong that might other-wise go unredressed." *In re Cadillac V8-6-4 Class Action*, 93 N.J. 412, 424, 461 A.2d 736 (1983). "If each victim were remitted to an individual suit, the remedy could be illusory, for the individual loss may be too small to warrant a suit.... Thus the wrongs would go without redress, and there would be no deterrence to further aggressions." *Riley v. New Rapids Carpet Ctr.*, 61 *N.J.* 218, 225, 294 *A.*2d 7 (1972). Other courts have referred to such small damage cases as "negative value" suits recognizing that they "would be uneconomical to litigate individually." *In re Monumental Life Ins. Co.*, 365 *F.*3d 408, 411 n. 1 (5th Cir.2004).

The class-action vehicle remedies the incentive problem facing litigants who seek only a small recovery. "[A] class action can produce a substantial fund to compensate ... [the class members'] attorney for his services." *In re Cadillac, supra*, 93 *N.J.* at 424, 461 *A.*2d 736. A "substantial fund" not only covers the attorney's actual fees, but also provides incentive in the form of possible contingency fees for attorneys to risk the prospect of receiving no recovery for their efforts. *See Amchem Products, Inc. v. Windsor*, 521 *U.S.* 591, 617, 117 *S.Ct.* 2231, 2246, 138 *L. Ed.*2d 689, 709 (1997) (stating that "[a] class action solves [the incentive problem created by small damages] by aggregating the relatively paltry potential recoveries into something worth someone's (usually an attorney's) labor."); *Eisen v. Carlisle & Jacquelin*, 417 *U.S.* 156, 161, 94 *S.Ct.* 2140, 2144, 40 *L. Ed.*2d 732, 739 (1974) (stating that "[n]o competent attorney would undertake this complex antitrust action to recover so inconsequential an amount [as $70]."). The class-action mechanism also overcomes the problem that small individual recoveries may fail to provide an adequate incentive for a litigant to investigate a claim or bring suit even if the litigant could secure representation. *See Varacallo v. Mass. Mutual Life Ins. Co.* .., 226 *F.R.D.* 207, 234 (D.N.J.2005) (stating that "[a]bsent class certification, very few individuals would

have the incentive ... to bring individual claims"). And, not least of all, there is the additional justification that a class-action proceeding "can aid the efficient administration of justice by avoiding the expense, in both time and money, of relitigating similar claims." *In re Cadillac, supra*, 93 *N.J.* at 435, 461 *A.*2d 736.

[10] In sum, the class-action mechanism is recognized to be valuable to litigants, to the courts, and to the public interest. Class actions fulfill the policies of this State even when only a small amount of damages is at stake. Not surprisingly, in light of the importance of its role generally, and specifically in recognition of its usefulness in connection with small-damages actions such as are often the case in consumer suits, this Court has instructed that "the class action rule should be construed liberally in a case involving allegations of consumer fraud." *Ibid.; see also* *Strawn v. Canuso*, 140 *N.J.* 43, 68, 657 *A.*2d 420 (1995) (stating that "a class action is the superior method for adjudication of consumer-fraud claims"); *Riley, supra*, 61 *N.J.* at 228, 294 *A.*2d 7 (stating that "a court should be slow to hold that a suit [under the CFA] may not proceed as a class action."). With those justifications for the class-action vehicle in mind we turn to consider the unconscionability of the contractual waiver of class-wide arbitration before us.

III.

A.

*8 [11] The arbitration agreement signed by Muhammad is clearly a contract of adhesion. We, therefore, must apply *Rudbart's* four factors, as did the Appellate Division, in order to determine whether New Jersey contract law principles permit enforcement of the class-arbitration prohibitions

found in the instant arbitration agreements.

[12] The first three factors of the *Rudbart* analysis require only brief attention. In respect of subject matter, the circumstantial backdrop to our *Rudbart* inquiry is the payday loan agreement executed between the parties. The focus of our analysis, however, is on the agreement's mandatory arbitration provision that contains limits on discovery and bars class-wide arbitration. In respect of *Rudbart's* second factor, the gross disparity in the relative bargaining positions of the parties is self-evident from the nature of the payday loan contract between a consumer and a financial entity.[FN4] We add only that the contract Muhammad entered into is, in its most general sense, a consumer contract. Although those facts, in addition to our finding that the contract is one of adhesion, indicate a degree of procedural unconscionability in Muhammad's contract, they are insufficient to render the contract unenforceable. That said, adhesive consumer contracts, which are ordinarily enforceable, nonetheless may rise to the level of unconscionability when substantive contractual terms and conditions impact "public interests" adversely.

Rudbart's fourth factor, the most important to the present analysis, considers "the public interests affected by the contract." That factor requires us to determine whether the effect of the class-arbitration bar is to prevent plaintiff from pursuing her statutory consumer protection rights and thus to shield defendants from compliance with the laws of this State. Those "public interest" considerations ultimately determine whether we can permit enforcement of the provision in plaintiff's contract that allegedly precludes any realistic challenge to the substance of her loan-contract's terms.

[13][14] In New Jersey, exculpatory waivers that seek a release from a statutorily imposed duty are void as against

public policy. *McCarthy v. NASCAR, Inc.*, 48 *N.J.* 539, 542, 226 *A.*2d 713 (1967). Muhammad's claims are statutory; however, the class-arbitration waiver at issue, and class-action waivers in general, are not, in the strictest sense of the term, exculpatory clauses. *See Discover Bank, supra*, 30 *Cal.Rptr.*3d 76, 113 *P.*3d at 1108. The class-arbitration waiver does not preclude Muhammad from filing an individual claim in arbitration. The difficulty lies in the fact that her individual consumer-fraud case involves a small amount of damages, rendering individual enforcement of her rights, and the rights of her fellow consumers, difficult if not impossible. In such circumstances a class-action waiver can act effectively as an exculpatory clause.

To permit the defendants to contest liability with each claimant in a single, separate suit, would, in many cases give defendants an advantage which would be almost equivalent to closing the door of justice to all small claimants. This is what we think the class suit practice was to prevent.

***9** [*Delgazzo v. Kenny*, 266 *N.J.Super.* 169, 193, 628 *A.*2d 1080 (App.Div.1993) (quoting *Hohmann v. Packard Instrument Co.*, 399 *F.*2d 711, 715 (7th Cir.1968)).]

Such waivers are problematic "when the waiver is found in a consumer contract of adhesion in a setting in which disputes between the contracting parties *predictably* involve small amounts of damages," as the California Supreme Court also recognized. *Discover Bank, supra*, 30 *Cal.Rptr.*3d 76, 113 *P.*3d at 1110 (emphasis added).

In most cases that involve a small amount of damages, "rational" consumers may decline to pursue individual consumer-fraud lawsuits because it may not be worth the time spent prosecuting the suit, even if competent counsel was willing to take the case. *See Kinkel v. Cingular Wireless, LLC*, 357 *Ill.App.*3d 556, 564, 293 *Ill.Dec.* 502, 828 *N.E.*2d 812, ---- (Ill.App.Ct.) (observing that in context of individually pursued small damage claims, any potential

recovery would be offset "by any costs incurred in presenting the claim and any lost wages for taking time from work to do so."), *appeal granted*, 216 *Ill.*2d 690, 298 *Ill.Dec.* 378, 839 *N.E.*2d 1025 (Ill.2005); *see also Carnegie v. Household Int'l, Inc.*, 376 *F.*3d 656, 661 (7th Cir.2004) (commenting that "only a lunatic or a fanatic sues for $ 30."). Moreover, without the availability of a class-action mechanism, many consumer-fraud victims may never realize that they may have been wronged. As commentators have noted,

> often consumers do not know that a potential defendant's conduct is illegal. When they are being charged an excessive interest rate or a penalty for check bouncing, for example, few know or even sense that their rights are being violated. Nor, given the relatively small amounts at stake, would most consumers find it worthwhile to seek legal advice to determine whether this is the case.

[Jean R. Sternlight and Elizabeth J. Jensen, *Mandatory Arbitration: Using Arbitration to Eliminate Consumer Class Actions: Efficient Business Practice or Unconscionable Abuse*, 67 *Law & Contemp. Prob.* 75, 88 (2004).]

[15] In addition to their impact on individual litigants, class-action waivers can functionally exculpate wrongful conduct by reducing the possibility of attracting competent counsel to advance the cause of action. Class-action waivers prevent an aggregate recovery that can serve as a source of contingency fees for potential attorneys. Although defendants have no obligation to provide counsel to plaintiff, they cannot take action that impedes ordinary citizens' access to representation to vindicate their rights. Defendants emphasize the availability of attorney's fees under the CFA; however, that fact is not dispositive in the instant case because the damages sought by Muhammad and those she seeks to represent are small. The availability of attorney's fees is illusory if it is unlikely that counsel would be willing

to undertake the representation. The finance charge for the loan in this matter was $60. The class of people whom plaintiff seeks to represent may have similar claims about that size. In fact, plaintiff had to roll-over her loan two times, bringing her compensatory claims to $180 that, with the possibility of treble damages available under CFA, may add up to a maximum of less than $600. One may be hard-pressed to find an attorney willing to work on a consumer-fraud complaint involving complex arrangements between financial institutions of other jurisdictions when the recovery is so small.[FN5] It cannot be that class-action waivers are less objectionable when a plaintiff is suing under a statute that *fails* to provide for attorney's fees (and damages multipliers). Such a perverse result would encourage under-enforcement of the very statutes that the Legislature has signaled as warranting strenuous enforcement.

***10** We hold, therefore, that the presence of the class-arbitration waiver in Muhammad's consumer arbitration agreement renders that agreement unconscionable. As a matter of generally applicable state contract law, it was unconscionable for defendants to deprive Muhammad of the mechanism of a class-wide action, whether in arbitration or in court litigation. The public interest at stake in her ability and the ability of her fellow consumers effectively to pursue their statutory rights under this State's consumer protection laws overrides the defendants' right to seek enforcement of the class-arbitration bar in their agreement.

We do not view our holding today to be at odds with the decision in *Gras v. Associates First Capital Co.*, 346 *N.J.Super.* 42, 786 *A.*2d 886 (App.Div.2001), *certif. denied*, 171 *N.J.* 445, 794 *A.*2d 184 (2002), in which the Appellate Division considered the issue before it to be whether class-action waivers were per se unenforceable. The court in *Gras, supra,* found that there was no "inherent conflict ... between arbitration and the underlying purpose of [the CFA]," 346

N.J.Super. at 52, 786 *A.*2d 886, and we agree. *Gras,* however, did not present the precise issue before the Court in this matter: whether the small amount of damages being pursued in this action involving complicated financial arrangements and multiple out-of-state entities effectively prevents plaintiff from being able to vindicate the public interests protected by the CFA.

[16] In our view, New Jersey's public policy favoring arbitration is not determinative of whether a specific class-arbitration waiver is unenforceable. Nothing in the arbitration process requires that claims be brought only by individuals. Moreover, unlike the limited discovery often found in arbitration agreements, class-arbitration waivers do not make arbitration a more streamlined and efficient forum for adjudicating disputes. One could speculate that class-arbitration waivers are viewed as more efficient because of the likelihood that fewer individual consumers would seek redress than those who would be included as part of a class. *Cf. Ting v. AT & T,* 182 *F.Supp.*2d 902, 931 n. 16 (N.D.Cal.2002) (stating that "the notion that it is to the public's advantage that companies be relieved of legal liability for their wrongdoing so that they can lower their cost of doing business is contrary to a century of consumer protection laws."), *aff'd in part, rev'd in part on other grounds,* 319 *F.*3d 1126 (9th Cir.2003). The purpose of arbitration, however, is not to discourage consumers from seeking vindication of their rights.

To be sure, many commentators have criticized, for various reasons, the class-action mechanism as it is applied in courts. *See* Sternlight and Jensen, *supra,* 67 *Law & Contemp. Prob.* at 102 (noting that "[a]cademics as well as corporate interests have pointed to ethical and efficiency issues and have argued that class actions be limited or reformed, if not eliminated."). Commentators have also suggested that class arbitration may in fact be no different or no more efficient

than class actions litigated in court. Jean R. Sternlight, *As Mandatory Arbitration Meets the Class Action, Will the Class Action Survive?*, 42 *Wm. and Mary L.Rev.* 1, 44-53 (2000); Jack Wilson, *No-Class-Action Arbitration Clauses, State Law Unconscionability, and the Federal Arbitration Act: A Case for Federal Judicial Restraint and Congressional Action*, 23 *Quinnipiac L.Rev.* 737, 773-80 (2004). In respect of court actions, the United States Congress and/or our State Legislature may amend class-action procedures should they perceive deficiencies in the current process. And, in the context of class arbitration, contracting parties and the various arbitration forums can fashion procedural rules specific to class arbitration. Class arbitration is in its infancy and may provide a fertile ground for establishing flexible class-action procedures. *See* *Discover Bank, supra*, 30 *Cal.Rptr.*3d 76, 113 *P.*3d at 1116 (discussing California's approach to class arbitration). The drafters of arbitration agreements and forum rules, as well as the arbitrators themselves, may allow for the development of innovative class-arbitration procedures that address some of the perceived inadequacies with the current system.[FN6] That said, in order for a specific procedure to be considered "class arbitration," we presume that the essential elements of modern class actions would be present.

B.

***11** Our decision today is rooted in the fact-sensitive public interest assessment of the *Rudbart* analysis and is not based on a determination that the arbitral forum, per se, cannot accomplish vindication of a consumer-fraud litigant's rights. In *Gilmer, supra*, the United States Supreme Court stated that arbitration is allowed in actions authorized by federal statutes "[s]o long as the prospective litigant effectively may vindicate [his or her] statutory cause of action in the arbitral forum." 500 *U.S.* at 28, 111 *S.Ct.* at 1653, 114 *L. Ed.*2d at 38

(quoting *Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc.*, 473 *U.S.* 614, 637, 105 *S.Ct.* 3346, 3359, 87 *L. Ed.*2d 444, 462 (1985)). That analysis was used again by the Court in *Green Tree Fin. Corp.-Alabama v. Randolph*, 531 *U.S.* 79, 90, 121 *S.Ct.* 513, 521, 148 *L. Ed.*2d 373, 383 (2000). Defendants argue that those holdings prevent the conclusion that we reach today in respect of Muhammad's arbitration agreement. We reject that argument.

Our analysis does not focus solely on the ability of Muhammad to individually vindicate her statutory rights. Our consideration of "the public interests affected by the contract" under *Rudbart* compels a broader inquiry into how class-action waivers affect the various interests protected under the CFA. Moreover, the analysis undertaken in *Gilmer* and *Randolph* reconciled various remedial federal statutes with the FAA. In *Randolph, supra,* the Court noted as part of its inquiry that it must "ask whether Congress has evinced an intention to preclude a waiver of judicial remedies for the statutory rights at issue." 531 *U.S.* at 90, 121 *S.Ct.* at 521, 148 *L. Ed.*2d at 383. That is a uniquely federal question, distinct from an analysis of *state* contract law under *Rudbart.* The California Supreme Court observed similarly in *Discover Bank, supra,* when examining federal cases that have applied *Gilmer* and *Randolph*, 30 *Cal.Rptr.*3d 76, 113 *P.*3d at 1114 n. 6. Noting the difference between the federal "vindication of statutory rights" test and an unconscionability analysis under state law, the California Supreme Court stated that the decisions following the former approach "address whether a federal statute impliedly limits arbitration, [and] are obviously not binding on this court when it decides whether class arbitration waivers are unconscionable under state law principles." *Ibid.; see also Kristian v. Comcast Corp.*, 446 *F.*3d 25, 60 n. 22 (1st Cir.2006) (concluding similarly that state unconscionability analysis, which is "based on the particulars of state contract law, may include considerations not present in the

vindication of statutory rights analysis .... which is not dependent on state law."); *In re: Universal Fund Telephone Billing Practices Litigation*, 300 *F.Supp.*2d 1107, 1136-38 (D.Kan.2003) (treating procedural unconscionability and availability of "[an] effective forum to vindicate statutory rights" as distinct inquiries).

C.

***12** [17][18][19][20] Finally, although we find that the class-arbitration waivers in Muhammad's arbitration agreements are unconscionable and unenforceable, we find that the waivers are severable. Once the waivers are removed, the remainder of the arbitration agreement is enforceable. As the Eleventh Circuit has explained,

[i]f all the provisions of the arbitration clause are enforceable, then the court must compel arbitration according to the terms of the agreement. If, however, some or all of its provisions are not enforceable, then the court must determine whether the unenforceable provisions are severable. Severability is decided as a matter of state law. If the offensive terms are severable, then the court must compel arbitration according to the remaining, valid terms of the parties' agreement. The court should deny the motion to compel arbitration only where the invalid terms of the arbitration clause render the entire clause void as a matter of state law.

[*Terminix Int'l Co. LP v. Palmer Ranch Ltd. P'ship*, 432 *F.*3d 1327, 1331 (11th Cir.2005) (citation omitted).]

Similarly, our courts have recognized that "[i]f a contract contains an illegal provision and such provision is severable, courts will enforce the remainder of the contract after excising the illegal portion, so long as the prohibited and valid provisions are severable." *Schuran, Inc. v. Walnut Hill*

Assocs., 256 *N.J.Super.* 228, 233, 606 *A.*2d 885 (Law Div.1991); *see also Naseef v. Cord, Inc.*, 90 *N.J.Super.* 135, 143, 216 *A.*2d 413 (App.Div.) (stating "[i]t is true that if a contract contains an illegal provision, if such provision is severable the courts will enforce the remainder of the contract after excising the illegal portion."), *aff'd*, 48 *N.J.* 317, 225 *A.*2d 343 (1966). The instant contracts embrace that proposition in that the broad class-action waivers in both contracts use the language "[t]o the extent permitted by law." Thus, the contracts reflect an intention that the arbitration agreement would be implemented whether and to whatever extent class-wide arbitration might be barred. Because we hold that the class-arbitration bar is not enforceable, we need not address plaintiff's additional argument about the impact of the discovery limitations on an individual arbitration claim.

IV.

The judgment of the Appellate Division is reversed and the matter is remanded to the Law Division for further proceedings consistent with this opinion.

Chief Justice PORITZ and Justices LONG, ZAZZALI, and WALLACE join in Justice LaVECCHIA's opinion. Justice RIVERA-SOTO filed a separate opinion concurring in part and dissenting in part. Justice ALBIN did not participate.Justice RIVERA-SOTO, concurring in part and dissenting in part.

To the extent the majority holds that the arbitration agreements in this case are enforceable, *ante*, --- *N.J.* ---- (2006) (slip op. at 32), I concur. However, to the extent the majority holds that the class-arbitration waivers in plaintiff's arbitration agreements are unconscionable, *ante*, --- *N.J.* ---- (2006) (slip op. at 26), I respectfully dissent for the reasons thoughtfully and exhaustively set forth by both the Appellate

Division, *Muhammad v. County Bank of Rehoboth Beach, Del.*, 379 *N.J.Super.* 222, 877 *A.*2d 340 (App.Div.2005), and the trial court.

For reversal and remandment-Chief Justice PORITZ and Justices LONG, LaVECCHIA, ZAZZALI and WALLACE-5.
For concurrence in part; dissent in part-Justice RIVERA-SOTO-1.
Not Participating-Justice ALBIN.

FN1. If the parties fail to agree on discovery matters, *NAF Rule* 29C allows mandatory discovery where the "cost [of discovery] is commensurate with the amount of the Claim." Muhammad contends that because her damages are only $180, limiting discovery to that amount, in the context of a complex claim, precludes her from obtaining relief.

FN2. The Appellate Division concluded that defendants had waived any argument that Delaware law should be applied (based on a choice of law clause in the contract). The panel found the issue to have been waived because it was not raised before the trial court and was raised only in a footnote in defendants' Appellate Division brief. *Muhammad, supra*, 379 *N.J.Super.* at 234 n. 3, 877 *A.*2d 340. Defendants did not seek review of the Appellate Division's determination of that issue.

FN3. This is not to say that when a contract of adhesion involves overwhelming procedural unconscionability, that those procedural factors are not included and weighed in the overall analysis for unconscionability. *See, e.g., Discover Bank, supra*, 36 *Cal.*4th 148, 30 *Cal.Rptr.*3d 76, 113 *P.*3d 1100 (finding gross unfairness in contract formation when

bill stuffer contained adhesion contract's terms). In that circumstance a "sliding scale" analysis may be appropriate. *See* Sitogum Holdings Inc., *supra*, 352 N.J.Super. at 565-66, 800 A.2d 915 (noting that courts have employed a "sliding scale" analysis when considering, in tandem, the two factors of procedural and substantive unconscionability).

FN4. The third *Rudbart* factor addresses the degree of economic compulsion motivating the "adhering" party. In respect of that factor we note only that payday loans may be necessities for persons who need access to cash and who may have credit difficulty, compelling their acquiescence to loans bearing exorbitant interest rates. Muhammad seeks to represent a class of people who, like herself, are under an allegedly high degree of economic compulsion to enter into such loan contracts.

FN5. In many respects, this is a fact-sensitive analysis and close cases may require the development of some proofs by a putative class plaintiff and fact-finding on the court's part. *See* Sternlight and Jensen, *supra*, 67 *Law & Contemp. Prob.* at 87 (stating that "[t]estimony from parties, local attorneys, or experts can establish which claims plaintiffs and their attorneys deem worth bringing. Such testimony needs to be specific as to what kinds of damages and attorney's fees would be available for individual claims [and] why these are insufficient"). At some point, an amount of damages will be high enough to attract counsel if attorney's fees are available, even though no counsel would take the same case if no attorney's fees were available. When "substantial damages" are at stake, the court should consider whether the availability of attorney's fees (including possible fee enhancement, *Rendine v. Pantzer*, 141

N.J. 292, 661 *A.*2d 1202 (1995)) in conjunction with a substantial potential damages award (including potential statutory multipliers) would allow a "substantial number" of consumers to obtain counsel and seek relief.

FN6. One objection lodged against class actions is that because the stakes are so high, defendants are pressured into settling arguably frivolous claims. The amicus Chamber of Commerce advances that concern, noting the "hydraulic pressure to settle that class certification creates." *See also In re Rhone-Poulenc Rorer Inc.*, 51 *F.*3d 1293, 1299-1300 (7th Cir.) (noting that class certification can force defendants to stake "their companies on the outcome of a single jury trial," whereas numerous individual trials would "reflect a consensus, or at least a pooling of judgment, of many different tribunals.") (Posner, J.), *cert. denied,* 516 *U.S.* 867, 116 *S.Ct.* 184, 133 *L. Ed.*2d 122 (1995); Myriam Gilles, *Opting Out of Liability: The Forthcoming, Near-Total Demise of the Modern Class Action,* 104 *Mich. L.Rev.* 373, 374 (2005) (noting criticism that class certification gives "outsized leverage" to "even the most baseless of class claims."); Wilson, *supra,* 23 *Quinnipiac L.Rev.* at 778 (stating in respect of class arbitration that "companies must fear that a 'renegade arbitrator' will enter an enormous judgment, which almost certainly would be subject to only the traditional, limited judicial review of arbitral awards."). Those concerns could be addressed through class-arbitration rules drafted to establish methods that spread the risks associated with a single decision-maker while still preserving many of the efficiencies of the modern class-action procedure.

N.J.,2006.
Muhammad v. County Bank of Rehoboth Beach, Delaware
--- A.2d ----, 2006 WL 2273448 (N.J.)

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Muhammad v. County Bank of Rehoboth BeachN.J.Super.A.D.,2005.

Superior Court of New Jersey,Appellate Division.

Jaliyah MUHAMMAD, on her own and on behalf of all others similarly situated, Plaintiff-Appellant,

v.

COUNTY BANK OF REHOBOTH BEACH, Delaware; Easy Cash; Telecash; and Main Street Corporation,[FN1] Defendants-Respondents.

FN1. Respondent County Bank certified that "Easy Cash" and "Telecash" were trade names that were used by County Bank in connection with the advertising and making of its short term loans. Main Street used the trade name "Easy Cash" but did not use the name "Telecash". They were not independent entities.

Argued March 15, 2005.

Decided July 14, 2005.

Background: Borrower brought class action against lender and servicer of payday loan, alleging that all defendants violated the New Jersey Consumer Fraud Act, the servicer violated usury law and the New Jersey Racketeer Influenced and Corrupt Organizations Act (RICO), and the lender conspired to violate RICO. Defendants moved to compel arbitration. The Superior Court, Law Division, Union County, granted motion. Borrower appealed.

Holdings: The Superior Court, Appellate Division, Falcone, J.A.D., held that:

(1) unequal bargaining power was not sufficient to render arbitration agreement unconscionable;

(2) borrower's economic duress was not sufficient to render agreement unconscionable;

(3) arbitration rule limiting discovery did not render agreement unconscionable; and

(4) agreement provision that precluded class actions did not render agreement unconscionable.

Affirmed.

Kestin, P.J.A.D., concurred and filed an opinion.

West Headnotes

[1] Appeal and Error 30 ⚿1078(1)

30 Appeal and Error
30XVI Review
30XVI(K) Error Waived in Appellate Court
30k1078 Failure to Urge Objections
30k1078(1) k. In General. Most Cited Cases

Borrower waived on appeal her argument that Delaware law applied to her action against lender, where she failed to brief the issue in the trial court.

[2] T ⚿113

25T Alternative Dispute Resolution
25TII Arbitration
25TII(A) Nature and Form of Proceeding
25Tk113 k. Arbitration Favored; Public Policy. Most Cited Cases
(Formerly 33k1.2 Arbitration)

T 138

25T Alternative Dispute Resolution
25TII Arbitration
25TII(B) Agreements to Arbitrate
25Tk136 Construction
25Tk138 k. Liberal or Strict Construction. Most Cited Cases
(Formerly 33k7.1 Arbitration)

T 139

25T Alternative Dispute Resolution
25TII Arbitration
25TII(B) Agreements to Arbitrate
25Tk136 Construction
25Tk139 k. Construction in Favor of Arbitration. Most Cited Cases
(Formerly 33k7.1 Arbitration)

A strong public policy exists favoring arbitration as a means of dispute resolution and requiring liberal construction of contracts in favor of arbitration.

[3] T 139

25T Alternative Dispute Resolution
25TII Arbitration
25TII(B) Agreements to Arbitrate
25Tk136 Construction
25Tk139 k. Construction in Favor of Arbitration. Most Cited Cases
(Formerly 33k7.1 Arbitration)

T 210

25T Alternative Dispute Resolution
25TII Arbitration

25TII(D) Performance, Breach, Enforcement, and Contest

25Tk204 Remedies and Proceedings for Enforcement in General

25Tk210 k. Evidence. Most Cited Cases

(Formerly 33k23.10 Arbitration)

The Federal Arbitration Act (FAA) establishes that, as a matter of federal law, any doubts concerning the scope of arbitrable issues should be resolved in favor of arbitration, whether the problem at hand is the construction of the contract language itself or an allegation of waiver, delay, or a like defense to arbitrability. 9 U.S.C.A. § 2.

[4] T 116

25T Alternative Dispute Resolution

25TII Arbitration

25TII(A) Nature and Form of Proceeding

25Tk116 k. What Law Governs. Most Cited Cases

(Formerly 33k2.2 Arbitration)

The Federal Arbitration Act (FAA) applies in state as well as federal courts. 9 U.S.C.A. § 2.

[5] T 137

25T Alternative Dispute Resolution

25TII Arbitration

25TII(B) Agreements to Arbitrate

25Tk136 Construction

25Tk137 k. In General. Most Cited Cases

(Formerly 33k7 Arbitration)

When deciding whether the parties agreed to arbitrate a certain matter including arbitrability, courts generally should apply ordinary state-law principles that govern the formation of contracts.

[6] Contracts 95 ⚿1

95 Contracts
95I Requisites and Validity
95I(A) Nature and Essentials in General
95k1 k. Nature and Grounds of Contractual Obligation. Most Cited Cases
When the issue of unconscionability is addressed, courts look at two factors, namely, unfairness in the formation of the contract, which is procedural unconscionability, and excessively disproportionate terms, which is substantive unconscionability.

[7] Contracts 95 ⚿1

95 Contracts
95I Requisites and Validity
95I(A) Nature and Essentials in General
95k1 k. Nature and Grounds of Contractual Obligation. Most Cited Cases
Procedural unconscionability can include a variety of inadequacies, such as age, literacy, lack of sophistication, hidden or unduly complex contract terms, bargaining tactics, and the particular setting existing during the contract formation process.

[8] Contracts 95 ⚿1

95 Contracts
95I Requisites and Validity
95I(A) Nature and Essentials in General
95k1 k. Nature and Grounds of Contractual Obligation. Most Cited Cases
Substantive unconscionability suggests the exchange of obligations so one-sided as to shock the court's conscience.

[9] Contracts 95 ⚿1

95 Contracts
95I Requisites and Validity
95I(A) Nature and Essentials in General
95k1 k. Nature and Grounds of Contractual Obligation. Most Cited Cases
A claim of unconscionability can succeed when one form of it, e.g., procedural unconscionability, is greatly exceeded, while the other form of it, e.g., substantive unconscionability, is only marginally exceeded.

[10] Contracts 95 ⚿1

95 Contracts
95I Requisites and Validity
95I(A) Nature and Essentials in General
95k1 k. Nature and Grounds of Contractual Obligation. Most Cited Cases
The issue of unconscionability is one of law for resolution by the court, and the burden of proving unconscionability is on the party asserting it.

[11] Contracts 95 ⚿1

95 Contracts
95I Requisites and Validity
95I(A) Nature and Essentials in General
95k1 k. Nature and Grounds of Contractual Obligation. Most Cited Cases
A "contract of adhesion" is presented on a take-it-or-leave-it basis, commonly in a standardized printed form, without opportunity for the adhering party to negotiate except perhaps on a few particulars.

[12] Contracts 95 ⚿1

95 Contracts
95I Requisites and Validity
95I(A) Nature and Essentials in General
95k1 k. Nature and Grounds of Contractual Obligation. Most Cited Cases
The mere fact that a contract is adhesive does not render it unenforceable.

[13] Contracts 95 ⚿1

95 Contracts
95I Requisites and Validity
95I(A) Nature and Essentials in General
95k1 k. Nature and Grounds of Contractual Obligation. Most Cited Cases
In determining whether to enforce the terms of a contract of adhesion, the appropriate analysis requires a consideration of the subject matter of the contract, the relative bargaining powers of each party, the degree of economic compulsion motivating the adhering party, and the public interests affected by the contract.

[14] T ⚿134(6)

25T Alternative Dispute Resolution
25TII Arbitration
25TII(B) Agreements to Arbitrate
25Tk131 Requisites and Validity
25Tk134 Validity
25Tk134(6) k. Unconscionability. Most Cited Cases
(Formerly 33k6.2 Arbitration)
Borrower's contention that the arbitration forum would not issue a binding, public opinion, and consequently would hide payday lender's alleged scheme to evade usury laws was

speculative and went against the strong policy favoring arbitration, and thus, it was insufficient to render arbitration clause in loan documents unconscionable.

[15] T 134(6)

25T Alternative Dispute Resolution
25TII Arbitration
25TII(B) Agreements to Arbitrate
25Tk131 Requisites and Validity
25Tk134 Validity
25Tk134(6) k. Unconscionability. Most Cited Cases
(Formerly 33k6.2 Arbitration)

Although borrower had unequal bargaining power in entering into payday loan with lender, such inequality was insufficient to render arbitration agreement in loan documents unconscionable, where there was no indication that borrower ever sought to alter the terms of the agreement and was precluded from doing so, or that lender's liability was limited.

[16] T 134(6)

25T Alternative Dispute Resolution
25TII Arbitration
25TII(B) Agreements to Arbitrate
25Tk131 Requisites and Validity
25Tk134 Validity
25Tk134(6) k. Unconscionability. Most Cited Cases
(Formerly 33k6.2 Arbitration)

Borrower was not under sufficient economic duress so as to render arbitration clause in payday loan documents unconscionable, even though at the time she obtained the loan she was experiencing financial stress, where no employee of lender solicited borrower or exerted pressure on

her to make any loan, and, in fact, borrower had approached lender for loan.

[17] T 134(6)

25T Alternative Dispute Resolution
25TII Arbitration
25TII(B) Agreements to Arbitrate
25Tk131 Requisites and Validity
25Tk134 Validity
25Tk134(6) k. Unconscionability. Most Cited Cases
(Formerly 33k6.2 Arbitration)

National Arbitration Forum rule that limited the cost of discovery in arbitration to the amount of the claim if the parties could not mutually agree on the discovery to be exchanged did not place borrower in any worse position than she would have been in if she were able to pursue her claim against lender in state court, and thus, rule did not render arbitration agreement unconscionable, where the rule did not place any more restrictive limits on the parties than the Rules of Court regarding actions in Small Claims Court and actually permitted more discovery than permitted by the court rules. R. 6:4-3(e).

[18] T 134(6)

25T Alternative Dispute Resolution
25TII Arbitration
25TII(B) Agreements to Arbitrate
25Tk131 Requisites and Validity
25Tk134 Validity
25Tk134(6) k. Unconscionability. Most Cited Cases
(Formerly 33k6.2 Arbitration)

T 361

25T Alternative Dispute Resolution
25TII Arbitration
25TII(H) Review, Conclusiveness, and Enforcement of Award
25Tk360 Impeachment or Vacation
25Tk361 k. In General. Most Cited Cases
(Formerly 33k6.2 Arbitration)

Assuming arbitration forum was biased in favor of lenders, borrower's interests were protected, and thus arbitration clause was not unconscionable, even though an arbitrator could not be removed before the award, given that the court was authorized to vacate an arbitration award if there was evidence of impartiality or corruption. 9 U.S.C.A. § 10(a)(2); N.J.S.A. 2A:24-8.

[19] T 134(6)

25T Alternative Dispute Resolution
25TII Arbitration
25TII(B) Agreements to Arbitrate
25Tk131 Requisites and Validity
25Tk134 Validity
25Tk134(6) k. Unconscionability. Most Cited Cases
(Formerly 33k6.2 Arbitration)

Arbitration agreement between borrower and lender, which precluded borrower from bringing class action against lender, was not unconscionable, where the agreement contained clear, consistent, and unambiguous language relating to the agreement to arbitrate all disputes and borrower's agreement not to bring, join, or participate in a class action.

[20] T 121

25T Alternative Dispute Resolution
25TII Arbitration
25TII(A) Nature and Form of Proceeding
25Tk118 Matters Which May Be Subject to Arbitration Under Law
25Tk121 k. Statutory Rights and Obligations. Most Cited Cases
(Formerly 33k3.3 Arbitration)
New Jersey Racketeer Influenced and Corrupt Organizations Act (RICO) claims are subject to arbitration.

[21] T 205

25T Alternative Dispute Resolution
25TII Arbitration
25TII(D) Performance, Breach, Enforcement, and Contest
25Tk204 Remedies and Proceedings for Enforcement in General
25Tk205 k. In General. Most Cited Cases
(Formerly 33k23.7 Arbitration)
Borrower was not entitled to conduct discovery prior to the determination of the validity of the arbitration clause in loan documents.

**342 *227 Donna Siegel Moffa, Philadelphia, PA, argued the cause for appellant (Williams, Cuker and Berezofsky and Trujillo Rodriguez & Richards, attorneys; Mark R. Cuker and Ms. Moffa, on the brief).
Marc J. Zucker, Philadelphia, argued the cause for the respondent County Bank (Weir & Partners attorneys; Susan Verbonitz and Mr. Zucker, on the brief).
Claudia T. Callaway (Paul, Hastings, Janofsky & Walker)of the District of Columbia Bar, admitted pro hac vice, argued

the cause for respondent Main Street Service Corp. (Sweeney & Sheehan, and Ms. Callaway, attorneys; Ms. Callaway of counsel; J. Michael Kunsch, on the brief).
Pinilis Halpern, attorneys for amicus curiae AARP Foundation and Counsel for National Association of Consumer Advocates (William J. Pinilis, of counsel and on the brief).

Before Judges KESTIN, LEFELT and FALCONE.

The opinion of the court was delivered by
**343 FALCONE, J.A.D.
The principal question presented in this interlocutory appeal, and one that appears to be of first impression in this State, is whether a mandatory arbitration provision in a payday loan contract is enforceable. A "payday loan" is a short term, single payment, unsecured consumer loan, so-called because payment is typically due on the borrower's next payday.

Plaintiff, Jaliyah Muhammad, contends that, because the arbitration clause is both procedurally and substantively unconscionable, the trial court erred in its determination that the clause was enforceable. She further contends that the trial court should have permitted discovery prior to making its determination that the arbitration clause is enforceable. We disagree and affirm.

*228 *I.*

Here are the pertinent facts and relevant procedural history. According to the certification of David E. Gillan, a Vice President of defendant, County Bank of Rehoboth Beach, Delaware (County Bank), County Bank is a federally insured depository institution, chartered under Delaware law, whose main office is located in Rehoboth Beach, Delaware. Since 1997, one of the products offered by County Bank is a

payday loan. An applicant may be approved for a loan of up to $500. County Bank uses independent servicers, including defendant Main Street Service Corporation (Main Street) to market its consumer loans nationally.

County Bank has entered into standardized written contracts with its servicers. Under the terms of these contracts, the servicers market the loans, assist in processing loan applications, and service and collect the loans, which are made and funded exclusively by County Bank and not the servicers. In 2003, Market Street operated a telephone service center located in Pennsylvania from which it marketed, processed, serviced and collected County Bank's loans in accordance with policies and procedures established by County Bank.

According to plaintiff, she was enrolled in 2003 as a part-time student at Berkley College in Paramus. Although her tuition was financed by student loans, she had other educational expenses, such as books, which were not covered by the loans. In April 2003, based on a need for cash to purchase books for her "next college terms", plaintiff responded to a Main Street advertisement. A loan application was faxed to her. On page two of the application, just above plaintiff's signature, were clauses entitled, "AGREEMENT TO ARBITRATE ALL DISPUTES" and "AGREEMENT NOT TO BRING, JOIN OR PARTICIPATE IN CLASS ACTIONS." The application further advised plaintiff that County Bank had "retained Main Street ... to assist in processing [her] Application and to service [her] loan." Plaintiff completed and returned the loan application by facsimile, seeking a $100 loan.

***229** Plaintiff also completed and returned by fax the one-page Loan Note and Disclosure form that included above her signature a number of clauses, including the following,

which are the subject of the dispute presented to us:
AGREEMENT TO ARBITRATE ALL DISPUTES: You and we agree that any and all claims, disputes or controversies between you and us and/or the Company, any claim by either of us against the other or the Company (or the employees, officers, directors, agents or assigns of the other or the Company) and any claim arising from or relating to your application for this loan or any other ****344** loan you previously, now or may later obtain from us, this Loan Note, this agreement to arbitrate all disputes, your agreement not to bring, join or participate in class actions, regarding collection of the loan, alleging fraud or misrepresentation, whether under the common law or pursuant to federal, state or local statute, regulation or ordinance, including disputes as to the matters subject to arbitration, or otherwise, shall be resolved by binding individual (and not joint) arbitration by and under the Code of Procedure of the National Arbitration Forum ("NAF") in effect at the time the claim is filed. This agreement to arbitrate all disputes shall apply no matter by whom or against whom the claim is filed. Rules and forms of the NAF may be obtained and all claims shall be filed at any NAF office, on the World Wide Web at www.arb-forum.com, by telephone at 800-474-2371, of at "National Arbitration Forum, P.O. Box 50191, Minneapolis, Minnesota 55405." Your arbitration fees may be waived by the NAF in the event you cannot afford to pay them. The cost of any participatory, documentary or telephone hearing, if one is held at your or our request, will be paid for solely by us as provided in the NAF Rules and, if a participatory hearing is requested, it will take place at a location near your residence. This arbitration agreement is made pursuant to a transaction involving interstate commerce. It shall be governed by the Federal Arbitration Act, 9 U.S.C. Sections 1-16. Judgment upon the award may be entered by any party in any court having jurisdiction.
NOTICE: YOU AND WE WOULD HAVE A RIGHT OR OPPORTUNITY TO LITIGATE DISPUTES THROUGH A

COURT AND HAVE A JUDGE OR JURY DECIDE THE DISPUTES BUT HAVE AGREED INSTEAD TO RESOLVE DISPUTES THROUGH BINDING ARBITRATION.

AGREEMENT NOT TO BRING, JOIN OR PARTICIPATE IN CLASS ACTIONS: To the extent permitted by law, you agree that you will not bring, join or participate in any class action as to any claim, dispute or controversy you may have against us, our employees, officers, directors, servicers and assigns. You agree to the entry of injunctive relief to stop such a lawsuit or to remove you as a participant in the suit. You agree to pay the attorney's fees and court costs we incur in seeking such relief. This Agreement does not constitute a waiver of any of your rights and remedies to pursue a claim individually and not as a class action in binding arbitration as provided above.

After this language, and just above the signature line, the following language appears: ***230** BY SIGNING BELOW, YOU AGREE TO ALL OF THE TERMS OF THIS NOTE, INCLUDING THE AGREEMENT TO ARBITRATE ALL DISPUTES AND THE AGREEMENT NOT TO BRING, JOIN OR PARTICIPATE IN CLASS ACTIONS. YOU ALSO ACKNOWLEDGE RECEIPT OF A FULLY COMPLETED COPY OF THIS NOTE.

The Loan Note and Disclosure form executed by plaintiff disclosed that the amount of the loan was $100, the finance charge was $30, the annual percentage rate (APR) was 644.1%, and payment of $130 from plaintiff was due on May 16, 2003.

On or about May 23, 2003, plaintiff applied for and received a payday loan of $200. The identical forms were executed by plaintiff. The Loan Note and Disclosure ****345** form for this loan disclosed that the amount of the loan was $200, the finance charge was $60, the APR was 608.33%, and

payment of $260 from plaintiff was due on June 13, 2003.[FN2]

> FN2. In her brief, plaintiff states that she "extended" this loan twice, each time paying an interest charge of $60 (for a total finance charge of $180 on a $200 loan). In the record presented, there is no documentation to support this claim. The record does support, however, that plaintiff made three payday loans.

On or about June 6, 2003, plaintiff applied for and received another payday loan of $200. Again, the paperwork was identical to the forms previously executed by plaintiff. The Loan Note and Disclosure form disclosed the amount of the loan, the finance charge of $60, the APR of 782.14%, and a repayment date of June 27, 2003.

As to all three loans, the exchange of paperwork between plaintiff and Main Street took place by facsimile and, once a loan application was approved, funds were transmitted from a County Bank account directly to plaintiff's checking account.

II.

On or about February 2, 2004, plaintiff filed a class action complaint alleging that: (1) all four defendants violated the New Jersey Consumer Fraud Act, N.J.S.A. 56:8-1 to -20; (2) Main Street, Easy Cash and Telecash violated the civil usury law, ***231** N.J.S.A. 31:1-1 to -9, and engaged in a pattern of racketeering in violation of N.J.S.A. 2C:41-1 to -6.2, the New Jersey Racketeering and Corrupt Organizations Act (RICO statute); and (3) County Bank conspired with the other defendants to violate the RICO statute, N.J.S.A. 2C:5-2, and aided and abetted the other defendants in conduct that

violated the civil and criminal usury laws of this State. Thereafter, on or about February 23, 2004, plaintiff made a demand upon defendants for the production of documents and propounded thirty-eight interrogatories.

On or about March 11, 2004, defendants removed the case to federal court on the ground that plaintiff's claims were preempted by federal law, 12 *U.S.C.A.* § 1831d, because they amounted to usury claims against a state-chartered bank. Five days later, defendants filed a motion to stay the action pending arbitration and to compel arbitration or, in the alternative, to dismiss the case. On or about April 1, 2004, while defendants' motion was pending, plaintiff filed a motion to remand the action to state court.

On or about May 18, 2004, U.S. Magistrate Judge Hedges issued a report wherein he recommended that plaintiff's remand motion should be granted. By written decision dated June 10, 2004, Federal District Court Judge Martini ordered remand of the matter to state court.

On or about July 7, 2004, defendants filed a notice of motion in state court to stay the action pending arbitration and to compel arbitration on the ground that "the parties entered into a written arbitration agreement which is governed by the Federal Arbitration Act, 9 *U.S.C.* § § 1-16, and provides for arbitration of claims such as those asserted [in the complaint]." Defendants also filed a notice of motion for a protective order on the grounds that discovery as to plaintiff's claims was "unwarranted and inappropriate" because the claims "[were] referable to arbitration pursuant to the parties written arbitration agreement...." Several weeks later, plaintiff filed a notice of cross-motion for an order striking defendants' objections to discovery and compelling responses to ***232** the interrogatories and production of documents requested in the discovery served on February 23, 2004.

**346 Prior to the return date of the motion and cross-motion, counsel for defendants wrote to plaintiff's counsel and expressed a willingness to participate in an American Arbitration Association (AAA) arbitration of plaintiff's individual claim, since plaintiff's brief in opposition to defendants' motion had suggested to defendants that plaintiff's rights "would be better protected in an arbitration conducted before the AAA as opposed to the NAF identified in the parties' arbitration agreement." In a response dated August 2, 2004, counsel for plaintiff emphatically declined this offer, characterizing it as "nothing more than a ploy to preserve advantages of an arbitration clause" and "an effort to prevent the court from scrutinizing a practice which [defendants] will repeat against other consumers who are not represented by counsel and who are not able to effectively challenge the cost issue."

III.

Defendants' motion for a stay of the action, to compel arbitration, and for a protective order, as well as plaintiff's cross-motion for an order striking defendants' objections to discovery, were argued before Judge Lyons on August 6, 2004. After reviewing New Jersey case law and declining to address the underlying dispute that plaintiff had with defendants as to the legality of payday loans, the motion judge identified the agreement between plaintiff and defendants as a contract of adhesion and noted that the issues presented were whether "the provisions in [the] contract are such that they are to be enforced on the procedural issue of arbitration ..." and whether the arbitration plan as "substantively put forth is such as to be unconscionable." Judge Lyons decided these issues in favor of defendants.

Immediately after Judge Lyons rendered his oral decision, a colloquy ensued between the court and counsel as to the

form of order. Counsel for plaintiff requested an opportunity to submit a form of order, which would dismiss the case without prejudice "so that [plaintiff] can take it up as a matter of right ... to the *233 Appellate Division." Over the objection of defendants' counsel, Judge Lyons permitted both sides to submit a letter brief as to the form of order.

By letter brief dated August 9, 2004, counsel for plaintiff asked Judge Lyons "to dismiss [the] case without prejudice rather than to stay [the] case indefinitely pending the outcome of arbitration proceedings." A proposed form of order was submitted with the letter brief. Counsel for defendants forwarded a proposed form of order with a letter brief, dated August 11, 2004, in which plaintiff's request was opposed.

By order dated August 18, 2004, Judge Lyons stayed plaintiff's action pending arbitration pursuant to § 3 of the FAA, compelled arbitration of plaintiff's claims pursuant to § 4 of the FAA, and denied plaintiff's request "to modify [the] order to provide for the dismissal of [the] case." That same day, Judge Lyons signed a protective order under *R.* 4:10-3a, which provides, in pertinent part, "[u]pon motion ... by the person from whom discovery is sought, and for good cause shown, the court may make [an] order which justice requires to protect a party or person from annoyance ... or undue burden or expense, ... (a) [t]hat the discovery not be had."

Plaintiff filed a timely motion for leave to appeal from these two orders, which we granted on October 4, 2004. Thereafter, by order dated January 5, 2005, we granted the application of AARP, Consumers League of New Jersey and National Association of Consumer Advocates to appear as *amici curiae*. *R.* 1:13-9.

**347 *IV.*

[1] On appeal, plaintiff contends that the trial court erred: (1) by ordering plaintiff to proceed to arbitration because the arbitration agreement is unenforceable under New Jersey law; and (2) by not permitting discovery prior to making the arbitration decision.[FN3] In support of her claim that the arbitration clause is ***234** unconscionable and, thus, unenforceable, plaintiff argues that the "arbitration provision at issue is a one-sided contract, unilaterally imposed upon financially distressed [and unsophisticated] consumers in a market devoid of choices." She argues further that the arbitration clause "requires that small claims be heard on an individual basis only, in a forum [NAF] lacking impartiality that operates under a cloak of confidentiality and so severely limits discovery that it denies consumers the ability [to] fully and fairly litigate their claims."

> FN3. In a footnote in their appellate brief, defendants contend that because the agreement between the parties contained a choice of law provision, *i.e.*, "[t]his note is governed by Delaware law", that the law of that state should apply. We note that this choice-of-law question was not briefed in the trial court or discussed by the trial judge in his ruling. It is "wholly improper" to raise the issue now in a footnote. *See Almog v. Israel Travel Advisory Serv., Inc.*, 298 *N.J.Super.* 145, 155, 689 *A.*2d 158 (App.Div.), *certif. granted*, 151 *N.J.* 463, 700 *A.*2d 876 (1997), *appeal dismissed*, 152 *N.J.* 361, 704 *A.*2d 1297, *cert. denied*, 525 *U.S.* 817, 119 *S.Ct.* 55, 142 *L.Ed.*2d 42 (1998).

In support of plaintiff, *amici* contend that, since the usury laws of New Jersey protect consumers, the arbitration clause should be invalidated because it is a way to "hide ...

exploitative business practices from public scrutiny and prevent vulnerable borrowers from obtaining redress and changing industry practices." In their joint brief, *amici* set forth the history and nature of payday loans and describe how lenders use exploitative practices that are costly to borrowers and exacerbate borrowers' problems with debt. They also discuss how lenders' relationships with out-of-state banks effectively evade state usury loans. While these claims are arguably compelling and raise important issues, they do not specifically address the issues before us, namely, the enforceability of the arbitration clause and the discovery question. We note, before addressing the issues presented, that if the practice of offering payday loans in this State is to be abolished, it will take legislative action to do so. *See* *Bankwest, Inc. v. Baker*, 324 *F.Supp.*2d 1333 (N.D.Ga.2004)(the Georgia law, *O.C.G.A.* § § 16-17-1 to 16-17-10, that declared payday loans illegal in that state was upheld as constitutional).

***235** [2] We have considered and analyzed the written and oral arguments of the parties and the brief submitted by *amici* and, applying prevailing legal principles and procedural standards, including the principle that "this State has a strong public policy 'favoring arbitration as a means of dispute resolution and requiring liberal construction of contracts in favor of arbitration' ", *Caruso v. Ravenswood Developers, Inc.*, 337 *N.J.Super.* 499, 504, 767 *A.*2d 979 (App.Div.2001)(quoting *Alamo Rent A Car, Inc. v. Galarza*, 306 *N.J.Super.* 384, 389, 703 *A.*2d 961 (App.Div.1997)), we reject plaintiff's claims and affirm.

V.

[3] Congress enacted the FAA, 9 *U.S.C.A.* § § 1-16, to "reverse longstanding judicial hostility" to arbitration agreements and to "place arbitration agreements upon the

same footing as other contracts." *Gilmer v. Interstate/Johnson Lane Corp.*, 500 *U.S.* 20, 24, 111 *S.Ct.* 1647, 1651, 114 *L.Ed.*2d 26, 36 (1991). The New Jersey counterpart to the FAA is **348*N.J.S.A.* 2A:24-1 to -11. In pertinent part, § 2 of the FAA provides:

A written provision in any ... contract evidencing a transaction involving commerce to settle by arbitration a controversy thereafter arising out of such contract or transaction or the refusal to perform the whole or any part thereof, or an agreement in writing to submit to arbitration an existing controversy arising out of such a contract, transaction, or refusal, shall be valid, irrevocable, and enforceable, save upon such grounds as exist at law or in equity for the revocation of any contract.

[9 *U.S.C.A.* § 2.]

See *N.J.S.A.* 2A:24-1. In *Southland Corp. v. Keating*, 465 *U.S.* 1, 10, 104 *S.Ct.* 852, 854, 79 *L.Ed.*2d 1, 12 (1984), the Supreme Court stated that § 2 of the FAA was enacted to establish a national policy "favoring" arbitration.The Arbitration Act establishes that, as a matter of federal law, any doubts concerning the scope of arbitrable issues should be resolved in favor of arbitration, whether the problem at hand is the construction of the contract language itself or an allegation of waiver, delay, or a like defense to arbitrability. [*Moses H. Cone Mem. Hosp. v. Mercury Constr. Corp.*, 460 *U.S.* 1, 24-25, 103 *S.Ct.* 927, 941, 74 *L.Ed.*2d 765, 785 (1983).]

*236 [4][5] While the FAA applies in state as well as federal courts, *Southland Corp., supra*, 465 *U.S.* at 12, 104 *S.Ct.* at 859, 79 *L.Ed.*2d at 13, "[g]enerally, contract defenses, such as fraud, duress, or unconscionability may be applied to invalidate arbitration agreements without contravening § 2." *Doctor's Assocs., Inc. v. Casarotto*, 517 *U.S.* 681, 686-87, 116 *S.Ct.* 1652, 1653, 134 *L.Ed.*2d 902, 908-09 (1996). *See also Gras v. Associates First Capital*

Corp., 346 *N.J.Super.* 42, 47, 786 A.2d 886 (App.Div.2001), *certif. denied*, 171 *N.J.* 445, 794 *A.*2d 184 (2002). Thus, "[w]hen deciding whether the parties agreed to arbitrate a certain matter (including arbitrability), courts generally ... should apply ordinary state-law principles that govern the formation of contracts." *First Options of Chicago, Inc. v. Kaplan*, 514 *U.S.* 938, 944, 115 *S.Ct.* 1920, 1924, 131 *L.Ed.*2d 985, 993 (1995).

[6][7][8][9] In this state, we recognize unconscionability as a basis for invalidating a contract. *See Saxon Constr. and Management Corp. v. Masterclean of North Carolina*, 273 *N.J.Super.* 231, 236, 641 *A.*2d 1056 (App.Div.)("It is equally well recognized that our courts may refuse to enforce contracts that are unconscionable or violate public policy"), *certif. denied*, 137 *N.J.* 314, 645 *A.*2d 142 (1994). But, "[t]here is no hard and fast definition of unconscionability." *Lucier v. Williams*, 366 *N.J.Super.* 485, 492, 841 *A.*2d 907 (App.Div.2004). In *Howard v. Diolosa*, 241 *N.J.Super.* 222, 230, 574 *A.*2d 995 (App.Div.), *certif. denied*, 122 *N.J.* 414, 585 *A.*2d 409 (1990), we described unconscionability as "overreaching or imposition resulting from a bargaining disparity between the parties, or such patent unfairness in the contract that no reasonable person not acting under compulsion or out of necessity would accept its terms." When the issue of unconscionability is addressed, we look at two factors, namely, unfairness in the formation of the contract (procedural unconscionability) and excessively disproportionate terms (substantive unconscionability). *Sitogum Holdings, Inc. v. Ropes*, 352 *N.J.Super.* 555, 564, 800 *A.*2d 915 (Ch.Div.2002). Procedural unconscionability "can include a variety of inadequacies, such as age, literacy, lack of sophistication, hidden or unduly ***237** complex contract terms, bargaining tactics, and the particular setting existing during the contract formation process."****349** *Ibid.* Substantive unconscionability "suggests the exchange of obligations so one-sided as to shock the court's conscience."

Id. at 565, 800 *A.*2d 915. Applying a "sliding scale" of unconscionability, a claim of unconscionability can succeed when one form of it, *e.g.,* procedural unconscionability, is greatly exceeded, while the other form of it, *e.g.,* substantive unconscionability, is only marginally exceeded. *Id.* at 565-67, 800 *A.*2d 915.

[10] The issue of unconscionability is one of law for resolution by the court, *Gladden v. Cadillac Motor Car Div., General Motors Corp.,* 83 *N.J.* 320, 337, 416 *A.*2d 394 (1980), and the burden of proving unconscionability is on the party asserting it, *Howard, supra,* 241 *N.J.Super.* at 230, 574 *A.*2d 995.

[11][12][13] Here, plaintiff contends that the agreement was a contract of adhesion and thus procedurally unconscionable. While it appears that the agreement between plaintiff and defendants is a contract of adhesion-"it is presented on a take-it-or-leave-it basis, commonly in a standardized printed form, without opportunity for the 'adhering' party to negotiate except perhaps on a few particulars", *Rudbart v. North Jersey Dist. Water Supply Comm'n,* 127 *N.J.* 344, 353, 605 *A.*2d 681, *cert. denied sub nom., First Fid. Bank v. Rudbart,* 506 *U.S.* 871, 113 *S.Ct.* 203, 121 *L.Ed.*2d 145 (1992)-"the mere fact that a contract is adhesive does not render it unenforceable." *Gras, supra,* 346 *N.J.Super.* at 48, 786 *A.*2d 886. In fact, a finding that a contract is one of adhesion is the "beginning, not the end, of the inquiry." *Rudbart, supra,* 127 *N.J.* at 354, 605 *A.*2d 681. In determining whether to enforce the terms of a contract of adhesion, the appropriate analysis requires a consideration of the subject matter of the contract, the relative bargaining powers of each party, the degree of economic compulsion motivating the adhering party, and the public interests affected by the contract. *Id.* at 356, 605 *A.*2d 681.

[14] We now analyze plaintiff's claim of unenforceability in light of the four *Rudbart* factors. The parties appear to agree that the subject matter of the agreement is arbitration. Plaintiff contends that the arbitration forum will not issue a binding, public opinion, and consequently will hide defendants' "scheme" to evade the usury laws of this State. Besides being somewhat speculative, this contention must be balanced against this State's strong policy favoring arbitration.

[15] Plaintiff argues on the second *Rudbart* factor that the relative bargaining position of the parties and "the very terms of the loan constitute evidence that payday borrowers have a high degree of economic compulsion and are desperate enough to accept almost any contract provision, no matter how unfavorable." In this regard, plaintiff characterizes herself as "untrained and unsophisticated" and claims she had "no real choice but to agree to arbitration" because all payday lenders include an arbitration clause. As to defendants, plaintiff contends that County Bank was a "repeat player" in the payday loan market with an understanding of how clauses imposing arbitration and banning class actions insulated it from liability.

To bolster her claim that disparities in knowledge can support a finding of unconscionability, plaintiff cites the *Lucier* case, 366 *N.J.Super.* at 485, 841 *A.*2d 907. In *Lucier,* the question presented to us was the enforceability of a limitation-of-liability provision in a home inspection contract, the effect of which was to limit the home buyer's potential recovery to one-half of the fee paid for the home inspection service.**350 The plaintiffs claimed damages of $10,000, but the limitation-of-liability provision in the form contract limited defendant's liability to $192.50. The contract also contained an enforceable arbitration clause.

We held the provision was unconscionable and therefore unenforceable. Our determination was based on a number of factors: (1) the document was a contract of adhesion that defendant refused to alter despite plaintiffs' protests; (2) the parties were in a grossly disproportionate***239** bargaining position; (3) the potential damage level was so nominal as to avoid almost all responsibility for the professional's negligence; and (4) the provision was "contrary to the state's public policy of effectuating the purpose of a home inspection contract to render reliable evaluation of a home's fitness for purchase and holding professionals to certain industry standards." *Lucier, supra,* 366 *N.J.Super.* at 493, 841 *A.*2d 907.

We are satisfied that plaintiff's reliance on *Lucier* is misplaced because the facts are distinguishable. While the disparity in bargaining position was a factor in our decision in *Lucier,* equally compelling was the finding that the provision was against public policy because it severely limited defendant's responsibility. Here, while there was certainly unequal bargaining power between the parties, disparity will not always render a contract unconscionable. *See Gilmer, supra,* 500 *U.S.* at 33, 111 *S.Ct.* at 1655, 114 *L.Ed.*2d at 41 ("Mere inequality in bargaining power ... is not sufficient reason to hold that arbitration agreements are never enforceable in the employment context"). *See also Martindale v. Sandvik, Inc.,* 173 *N.J.* 76, 90, 800 *A.*2d 872 (2002)("Virtually every court that has considered the adhesive effect of arbitration provisions in employment applications or employment agreements has upheld the arbitration provision contained therein despite potentially unequal bargaining power between the employer and employee").

In addition, there is nothing in the record presented to us to establish that plaintiff ever sought to alter the terms of the agreement and was precluded from doing so, or that

defendants' liability was limited. It seems clear that plaintiff had the opportunity and ability to read the plain language of the agreement and was fairly apprised that she was not giving up, as she claims, her ability to vindicate her rights. Rather, plaintiff was agreeing to have the opportunity to vindicate those rights in an arbitration and not a court. *See Van Syoc v. Walter*, 259 *N.J.Super.* 337, 339, 613 *A.*2d 490(App.Div.1992)("when ... parties agree to arbitrate, they are opting for a nonjudicial manner of resolving their disputes", ***240** and "[i]t is not whether the contract can be attacked, but the forum in which the attack is to take place)", *certif. denied*, 133 *N.J.* 430, 627 *A.*2d 1136 (1993).

[16] Regarding the third *Rudbart* factor, plaintiff contends that economic duress forced her to make the agreement in order "to cover immediate expenses for which she had no cash." "Economic duress occurs when the party alleging it is 'the victim of a wrongful or unlawful act or threat', which 'deprives the victim of his [or her] unfettered will.' " *Quigley v. KPMG Peat Marwick, LLP*, 330 *N.J.Super.* 252, 263, 749 *A.*2d 405 (App.Div.)(quoting 13 *Williston on Contracts*, § 1617 (Jaeger ed.1970)), *certif. denied*, 165 *N.J.* 527, 760 *A.*2d 781 (2000). In *Continental Bank v. Barclay Riding Academy, Inc.*, 93 *N.J.* 153, 177, 459 *A.*2d 1163, *cert. denied*, 464 *U.S.* 994, 104 *S.Ct.* 488, 78 *L.Ed.*2d 684 (1983), we noted "that the 'decisive factor' is the wrongfulness of the pressure exerted [,]" and that "[t]he term 'wrongful' ... encompasses more than criminal or tortuous acts, for conduct ****351** may be legal but still oppressive." Further, wrongful acts can include acts that are wrong in a moral or equitable sense. *Ibid.*

In *Quigley, supra*, 330 *N.J.Super.* at 252, 749 *A.*2d 405, plaintiff claimed that the trial court erred in enforcing an arbitration agreement that she had signed after having been advised by her supervisor that she would be terminated if she declined to sign. In reversing the trial court, we stated that

"courts that have considered this issue [of whether the threat of termination of employment for refusing to agree to arbitration is oppressive] have consistently determined that the economic coercion of obtaining or keeping a job, without more, is insufficient to overcome an agreement to arbitrate statutory claims." *Id.* at 264, 749 *A*.2d 405. We made a finding that plaintiff had not demonstrated more than ordinary economic pressure faced by every employee who needed a job and concluded that there was no economic duress to render the arbitration agreement unconscionable. *Id.* at 266, 749 *A*.2d 405.

***241** We are satisfied here that plaintiff's circumstances are less compelling than an employee who is forced to sign an arbitration agreement as a condition of continued employment. Plaintiff was not the victim of a wrongful or unlawful act or threat. She was simply a person who needed money to purchase school books and decided to meet this expense by making a number of payday loans. No employee of the defendants solicited plaintiff or exerted pressure on her to make any of the loans. Indeed, plaintiff approached the defendants. And, while plaintiff may have been experiencing financial stress, she was not, under these facts, the victim of sufficient economic duress to render the arbitration clause she signed unconscionable.

As to the final *Rudbart* factor, *i.e.*, whether a contract of adhesion is unconscionable because the public interest is affected by the agreement, plaintiff contends that: (A) the procedural limitations on the chosen forum, NAF, especially NAF rules 37 and 29, preclude her from a full and fair opportunity to litigate her claim; (B) that NAF is biased; and (C) the arbitration clause is exculpatory in that it denies the borrower the right to participate in a class action suit.

A.

In regard to NAF procedures, plaintiff argues that they are defective because they are confidential and do not permit *stare decisis* or collateral estoppel. She specifically objects to NAF Rule 37G (Awards), which provides that an award shall not include any reasons, findings of fact or conclusions of law unless requested and an additional fee of $100 is paid, and NAF Rule 29 (Discovery), which limits discovery to "an amount commensurate with the claim-even if the claim involves complex legal and factual issues." These claims are without merit. Because plaintiff is unable to establish precedents through her arbitration, this claimed "defect" does not render the forum violative of public policy, especially considering our strong policy favoring arbitration.

242** As to NAF Rule 37G, plaintiff has not explained why its terms preclude her from a full and fair opportunity for her claims to be heard. Plaintiff's conclusionary statement and lack of supporting legal argument as to this rule make it impossible for us to consider this issue. *See* Miller v. Reis, 189 *N.J.Super.* 437, 441, 460 *A.*2d 210 (App.Div.1983)(appellants' request for a declaration of third-party defendant's liability on a minor issue was not considered on appeal because the issue was raised in a conclusionary statement by the brief writer, but was not briefed). *See also* ****352State v. Hild*, 148 *N.J.Super.* 294, 296, 372 *A.*2d 642 (App.Div.1977).

[17] As noted, plaintiff argues that NAF Rule 29 precludes her from effectively litigating her small value claim. She maintains that defendants acted in concert through a complex legal arrangement to evade New Jersey's usury laws by means of a "rent-a-charter" scheme, whereby County Bank lent its Delaware charter to Main Street to enable Main Street to do business in this State without being subject to our usury laws. In order to prove the scheme, plaintiff

contends she will need extensive discovery. This issue is likewise without merit.

NAF Rule 29A provides, in pertinent part, "[p]arties shall cooperate in the exchange of documents and information[,]" and any party "requesting discovery shall contact other [p]arties and discuss discovery [r]equests and any objections and arrange for the exchange of documents and information." In pertinent part, NAF Rule 29B provides:
If the parties are unable to resolve discovery matters under Rule 29A, a Party may request the disclosure of documents, sworn answers to not more than twenty-five (25) written questions, or one or more depositions before a Hearing where:
1. The information sought is relevant to a Claim or Response, reliable, and informative to the Arbitrator;
2. The cost is commensurate with the amount of the Claim; and
3. The Request is reasonable and not unduly burdensome and expensive.

Pursuant to NAF Rule 29C, a party may request other discovery, including requests for admissions and requests for physical or mental examinations under the same three conditions listed under Rule 29B. And, under NAF Rule 29G, the arbitrator "may draw ***243** an unfavorable, adverse inference or presumption from the failure of a party to provide discovery" and may assess "costs, expenses, and fees, including reasonable attorney fees related to seeking or resisting discovery under [the rule] ... against the non-prevailing party."

The plain language of NAF Rule 29 makes it clear that the cost of discovery cannot exceed the amount of the claim, but this limitation is imposed only if the parties cannot mutually agree on the discovery to be exchanged. Despite this

apparent limitation on discovery, we are satisfied that Rule 29 does not place any more restrictive limits on the parties than do our Rules of Court regarding actions filed in Small Claims Court and, indeed, may permit more discovery than permitted by the court rules. Under NAF Rule 29, discovery is limited to the amount in controversy only if the parties are unable to resolve discovery issues between themselves. In these circumstances, the arbitrator may order answers to twenty-five interrogatories, "one or more depositions", and impose costs and sanctions if the non-producing party acted in bad faith. Under *R.* 6:4-3(e), "each party may serve interrogatories consisting of no more than five questions without parts." There are, however, no provisions for depositions or counsel fees. In these circumstances, since the limited discovery provided by NAF Rule 29 does not place plaintiff in any worse position than she would be in if she were able to pursue her claim in state court, her claim that the arbitration provision is unconscionable must fail.

B.

[18] Plaintiff claims that the arbitration clause is unconscionable because the chosen forum, NAF, is biased against consumers who bring suit against lenders. In response to this claim, defendants point to ****353** a number of reported decisions where the issue of NAF's bias was raised and rejected. *See* *Marsh v. First USA Bank, N.A.*, 103 *F.Supp.*2d 909 (N.D.Tex.2000); *Bank One, N.A. v. Coates*, 125 *F.Supp.*2d 819 (S.D.Miss.2001), *aff'd*, 2002 *WL* 663804 (5th Cir.2002); *Hutcherson v. Sears, Roebuck & Co.*, 342 ***244** *Ill.App.*3d 109, 276 *Ill.Dec.* 127, 793 *N.E.*2d 886, *appeal denied*, 205 *Ill.*2d 582, 281 *Ill.Dec.* 78, 803 *N.E.*2d 482 (2003).

In *Marsh*, the plaintiffs alleged that the NAF could not provide fair, impartial and effective relief because the NAF

was prejudiced against consumers and engaged in a collusive effort with lenders to defeat consumer claims. The plaintiffs pointed to statistics which indicated that the bank had prevailed against holders of its credit cards in the overwhelming majority of disputes resolved through NAF. In further support of their claim of bias, plaintiffs pointed to NAF's reluctance to disclose information to its arbitrators, NAF's exorbitant or indeterminate fees, and NAF's ability to change its code of procedure at the whim of its director.

In finding the plaintiffs' allegations unfounded, the court in *Marsh* was "satisfied that NAF will provide a reasonable, fair, and impartial forum" for the plaintiffs to seek redress of their grievances. The court noted that NAF's Code of Procedure and Code of Conduct had provisions addressing conflicts of interest, disqualification of potential arbitrators, and peremptory challenges. Further, the court noted that an arbitration was subject to review by the court under 9 *U.S.C.A.* § 10.

Here, we are satisfied that plaintiff's interests are protected, since, under 9 *U.S.C.A.* § 10(a)(2) and *N.J.S.A.* 2A:24-8, even though an arbitrator may not be removed before the award, a court may vacate an arbitration award if there is evidence of impartiality or corruption.

C.

[19] Plaintiff contends that the arbitration clause is unconscionable and contrary to public policy because it denies the borrower the right to participate in a class action suit, "effectively leaving payday borrowers without a realistic remedy." While plaintiff "does not contend that all contractual arbitration provisions that preclude aggregation of claims are unconscionable", she does allege "that in these circumstances, the preclusion [of class ***245** action suits]

supports a finding of unconscionability based on the totality of the circumstances."

In support of her contention, plaintiff cites to numerous out-of-state cases, including several cases submitted since oral argument under *R.* 2:6-11, to support her claim that preclusion of class action suits can invalidate an arbitration case. Since we discern no basis to depart from *Gras, supra,* 346 *N.J.Super.* at 45, 786 *A.*2d 886, which directly addresses the issue, we see no need to discuss these cases, except for two New Jersey cases, *Rockel v. Cherry Hill Dodge,* 368 *N.J.Super.* 577, 847 *A.*2d 621 (App.Div.), *certif. denied,* 181 *N.J.* 545, 859 *A.*2d 689 (2004) and *Discover Bank v. Shea,* 362 *N.J.Super.* 200, 827 *A.*2d 358 (Law Div.2001), cited by plaintiff to support her claim that Judge Lyons overstated the holding of *Gras.*

In *Gras,* the plaintiffs filed suit against finance companies claiming that the credit life insurance provisions in their loan agreements violated the New Jersey Consumer Fraud Act (CFA), *N.J.S.A.* 56:8-1 to -20. The defendants filed a demand for arbitration pursuant to the arbitration agreement contained in the loan documents signed by plaintiffs. The plaintiffs moved to stay the arbitration and the defendants cross-moved for a stay pending ****354** arbitration. The motion judge granted the defendants' motion and dismissed the plaintiffs' complaint. The plaintiffs appealed, claiming that the arbitration agreement was void because it contravened public policy by precluding class actions.

On appeal, after reviewing a number of federal cases that held the preclusion of class actions did not preclude arbitration and a number of cases cited by the plaintiffs for the contrary position and, finding the plaintiffs' authority "not persuasive", we rejected their claim. We noted, in affirming the motion judge, that "two significant public policies must be harmonized", namely, the CFA's policy to

"root out consumer fraud" and the "competing and compelling public policy favoring arbitration as a means of dispute resolution and requiring liberal construction of contracts in favor ***246** of arbitration." *Id.* at 53-54, 786 *A.*2d 886. In resolving the conflict, we stated:

On balance, even if we consider the policies in equipoise, we must consider that here the parties have agreed to permit the issues to be resolved in the arbitration forum. We recognize that the parties were in distinctly different bargaining positions. We are less certain of the economic compulsion that caused plaintiffs to recast each loan with a new loan over a short period of time. Nevertheless, even assuming that these factors ultimately favor plaintiffs' position, the absence of a legislative mandate or overriding public policy in favor of class actions leads us to conclude that the arbitration provision here is enforceable.

[*Id.* at 54, 786 *A.*2d 886.]

We are satisfied that plaintiff's reliance on *Rockel, supra,* 368 *N.J.Super.* at 577, 847 *A.*2d 621, is misplaced. There, we noted that the "arbitration agreement [was] highly ambiguous because the parties executed two documents which contain separate and somewhat disparate arbitration clauses", and concluded "that the uncertain content of the parties' agreement to arbitrate, the contracts' conflicting descriptions of the manner and procedure which would govern the arbitration proceedings, the absence of a definitive waiver of plaintiffs' statutory claims, and the obscure appearance and location of the arbitration provisions, militate against the entry of an order requiring arbitration over plaintiffs' objection." *Id.* at 580-81, 847 *A.*2d 621. In reversing the trial court's dismissal of the plaintiffs' complaint, we noted the distinctions between the provisions in question and those considered in *Gras* and held that the ambiguity in the arbitration agreement was "fatal to the compelling of the arbitration of plaintiffs' CFA claims."

Id. at 581, 847 *A.*2d 621. Finally, we note the following, which clearly distinguishes *Rockel* from *Gras* and supports defendants' position in this case:

The delicate balance between the policies of the CFA and the policy in favor of arbitration requires that the consumer be given reasonable notice of such provisions, that the provisions contain a clear waiver of statutory rights, and that the arbitration agreement be phrased in unambiguous terms. As explained, the arbitration agreement in question fails to meet these critical requirements. While we continue to adhere to *Gras's* holdings that arbitration may be compelled in a consumer transaction even when imposed by a party possessing superior bargaining power, and that a party claiming a contract to be the product of unconscionable conduct prohibited by the CFA may be compelled to arbitrate because of the presence of an arbitration clause contained in the very contract under attack, we ***247** conclude that any attempt to impose arbitration ****355** through an arbitration agreement less clear and less noticeable than that considered in *Gras* is not likely to pass muster. Here, the presence of two conflicting arbitration provisions, the expression of a waiver of the right to trial by jury in small print, and the absence of any other clear warning or caution of the waiver of statutory rights, requires a rejection of these claims.

[*Id.* at 587, 847 *A.*2d 621.]

Here, the factors noted in *Rockel,* which militate against mandatory arbitration, are not present. The loan application and the loan note and disclosure form faxed to plaintiff contain clear, consistent, and unambiguous language relating to the parties' agreement to arbitrate all disputes and plaintiff's agreement not to bring, join or participate in class actions. Both forms set forth in capital letters, above plaintiff's signature, a notice that the parties agreed to resolve all disputes through binding arbitration. And, the loan note

and disclosure set forth in capital letters an acknowledgment by plaintiff that by signing the form she was agreeing to arbitrate all disputes and agreeing not to bring, join or participate in class actions.

We are also satisfied that plaintiff's reliance on *Discover Bank, supra,* 362 *N.J.Super.* at 200, 827 *A.*2d 358, is equally unavailing. There, the plaintiff brought an action in New Jersey to compel arbitration against a defendant who had filed a class action against the plaintiff in California on behalf of the bank's credit card customers who had allegedly been charged improper overlimit fees. The plaintiff's demand to compel arbitration was denied and its complaint was dismissed. It appears that the original agreement between the credit cardholder and the bank did not contain an arbitration clause, but the bank amended its credit card agreement by way of a "bill stuffer" notice to provide for arbitration and to force its cardholders to give up their right to file a class action. Any cardholder who did not accept the new terms would have their account closed by the bank. In these circumstances, including a finding that the bank was able to "completely avoid accountability whenever the harm to each class member is small enough", the trial court concluded that the arbitration ***248** agreement was unenforceable and the agreement precluding class actions was unconscionable and unenforceable.

Discover Bank is clearly distinguishable from the case presented to us. First, unlike *Discover Bank* where the consumer received "notice" via a "bill stuffer", plaintiff in this case was clearly notified that she waived her right to file a class action. Second, we note that *Discover Bank,* which is a Law Division opinion, was decided two months prior to our decision in *Gras* and, to the extent it is in conflict with our holding in *Gras,* it is the latter that controls.

[20] Before addressing plaintiff's final argument that discovery was necessary, we note that plaintiff's contention that the agreement is unenforceable because her RICO claim cannot be vindicated in arbitration is clearly without merit. RICO claims are subject to arbitration. *Caruso, supra*, 337 *N.J.Super.* at 505, 767 *A.*2d 979; *Gras, supra*, 346 *N.J.Super.* at 52, 786 *A.*2d 886. *See also Republic of the Philippines v. Westinghouse Elec. Corp.*, 714 *F.Supp.* 1362, 1373 (D.N.J.1989).

VII.

[21] Plaintiff contends that Judge Lyons erred in ruling that the matter should proceed to arbitration without first permitting discovery. In support of her claim that discovery should have been permitted prior to the determination as to the validity of the arbitration clause, plaintiff ****356** cites *Blair v. Scott Specialty Gases*, 283 *F.*3d 595 (3d Cir.2002) and *Hayes v. County Bank*, 185 *Misc.*2d 414, 713 *N.Y.S.*2d 267 (2000). While the court permitted some limited discovery in each of these cases, we decline to adopt that approach as a requirement in this case. "Arbitration can attain its goal of providing final, speedy and inexpensive settlement of disputes only if judicial interference is minimized." *Barcon Associates v. Tri-County Asphalt Corp.*, 86 *N.J.* 179, 187, 430 *A.*2d 214 (1981). Here, plaintiff has not convinced us that discovery was needed before Judge Lyons made his decision that the matter should proceed to arbitration.

***249** *VIII.*

In summary, we are satisfied that plaintiff has failed to meet her burden that the contract was unconscionable and therefore unenforceable. We are equally satisfied that

plaintiff can vindicate her claims in arbitration. Accordingly, the orders of August 18, 2004 are affirmed.

KESTIN, P.J.A.D., concurring.

While concurring with the result, I respectfully depart from the majority's approach in this case. Because of plaintiff's rejection of defendants' offer to arbitrate the matter under the aegis of the American Arbitration Association and pursuant to its established rules and procedures, I would not consider any of plaintiff's arguments addressed to the validity of NAF's arbitration procedures. Having forgone the opportunity to avoid the asserted bias and procedural unconscionability inflicted by NAF arbitration standards, plaintiff should not now be heard to attack those very processes, which she, for a second time, elected to be bound by.

On a more basic level, I share the majority's views in resolving the conflict between two public policies: on the one hand, the rules permitting class actions and the standards governing them; and, on the other hand, our system's commitment to arbitration as an alternative remedial choice to litigation. I see no enforceable bar to plaintiff's right to raise, in arbitration, the important public policies she advances stemming from this State's usury laws or any other pertinent question of law she may choose to argue.

N.J.Super.A.D.,2005.
Muhammad v. County Bank of Rehoboth Beach
379 N.J.Super. 222, 877 A.2d 340

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Aug 18 2004
Thomas C. Lyons
J.S.C.

WEIR & PARTNERS LLP
A Pennsylvania Limited Liability Partnership
Susan Verbonitz, Esquire
Marc J. Zucker, Esquire
20 Dings Highway West
Haddonfield, New Jersey 08033
(856) 740-1490
Attorneys for County Bank of Rehoboth Beach, Delaware

SWEENEY & SHEEHAN, P.C.
J. Michael Kunsch, Esquire
Sentry Office Plaza, Suite 500
216 Haddon Avenue
Westmont, NJ 08108
(856) 869-5600

PAUL, HASTINGS, JANOFSKY & WALKER LLP
Claudia T. Callaway, Esquire
Pro hac vice
1299 Pennsylvania ,Avenue, N.W., Tenth Floor
Washington, D.C. 20004
(202) 508-9500
Attorneys for Main Street Service Corp.

JALIYAH MUHAMMAD, on her own behalf and all others similarly situated, Plaintiff,	: SUPERIOR COURT OF NEW JERSEY UNION COUNTY
	: Docket No. UNNL-0410-04
v.	: CIVIL ACTION
COUNTY BANK OF REHOBOTH BEACH, DELAWARE, EASY CASH TELECASH AND MAIN STREET SERVICE CORPORATION, JOHN DOE AND JOHN ROE, Defendants	: ORDER STAYING ACTION PENDING ARBITRATION AND COMPELLING ARBITRATION

This matter having come before the Court on the Motion of Weir & Partners LLP, counsel for County Bank of Rehoboth Beach, Delaware, and Sweeney & Sheehan, P.C_ and Claudia T. Callaway, Esquire of Paul, Hastings, Janofsky & Walker LLP, counsel for Main Street Service Corp., for an order staying this action pending arbitration pursuant to §3 of the Federal Arbitration Act (the "FAA"), 9 U.S.C. §3, and compelling arbitration of plain6Ts claims pursuant to §4 of the FAA, and the Court having considered the moving papers and response thereto, and for good cause shown,

It is on this 18 day of August, 2004, ORDERED that defendants' motion is GRANTED and this case is STAYED pending arbitration of the plaintiff's claims.

IT IS FURTHER ORDERED that, should plaintiff choose to pursue claims against defendants, she is directed to

do so in arbitration. The Court retains jurisdiction pending any such arbitration proceeding.

IT IS FURTHER ORDERED that plaintiff's request to modify this order to provide for the dismissal of this case is denied.

A copy of this order shall be served upon all counsel within seven (7) days of the date hereof.

BY THE COURT

/s/
Thomas C. Lyons, J.S.C.

THIS MOTION WAS OPPOSED:

x

THIS MOTION WAS UNOPPOSED:

Delta Funding Corp. v. HarrisN.J.,2006.--- A.2d ----Only the Westlaw citation is currently available.

Supreme Court of New Jersey.

DELTA FUNDING CORPORATION, Plaintiff-Respondent,

v.

Alberta HARRIS, Defendant-Appellant.

Argued Feb. 14, 2006.

Decided Aug. 9, 2006.

SYNOPSIS

Background: Sub-prime mortgage lender brought action, in federal court, to compel arbitration of borrower's state court claims, which named lender as a third-party defendant in foreclosure proceedings alleging lender violated the New Jersey Consumer Fraud Act. Borrower moved for summary judgment. The United States District Court for the District of New Jersey, 396 F.Supp.2d 512, denied borrower's motion for summary judgment, and compelled arbitration. Borrower appealed. The United States Court of Appeals for the Third Circuit certified a question to the New Jersey Supreme Court.

Holdings: The Supreme Court, LaVecchia, J., held that:

(1) cost-shifting provision in arbitration clause could be unconscionable, depending on arbitrator's interpretation of the provision;

(2) attorney fee provision in arbitration clause could be unconscionable, depending on arbitrator's interpretation of the provision;

(3) class-arbitration waiver was not unconscionable;

(4) arbitration clause's exclusion of foreclosure actions from

arbitration was not unconscionable, though borrower could be force to litigate similar claims in different forums.

Certified question answered.

Zazzali, J., filed an opinion concurring in part and dissenting in part.

Rivera-Soto, J., filed a dissenting opinion.

[1] Federal Courts 170B 392

170B Federal Courts
170BVI State Laws as Rules of Decision
170BVI(B) Decisions of State Courts as Authority
170Bk388 Federal Decision Prior to State Decision
170Bk392 k. Withholding Decision; Certifying Questions. Most Cited Cases
Purpose of the certification process, under which the New Jersey Supreme Court may answer a question of law certified by the United States Court of Appeals for the Third Circuit, is to answer the question of law submitted pursuant to the certification, not to resolve factual disputes between the parties. R. 2:12A-1.

[2] Alternative Dispute Resolution 25T 200

25T Alternative Dispute Resolution
25TII Arbitration
25TII(D) Performance, Breach, Enforcement, and Contest

25Tk197 Matters to Be Determined by Court
25Tk200 k. Arbitrability of Dispute. Most Cited Cases

Under federal arbitration law, it is ordinarily the role of an arbitrator and not the courts to interpret ambiguous provisions of an arbitration agreement, and that general rule is especially applicable where the arbitration agreement contains sweeping language concerning the scope of the questions committed to arbitration.

[3] Alternative Dispute Resolution 25T 134(6)

25T Alternative Dispute Resolution
25TII Arbitration
25TII(B) Agreements to Arbitrate
25Tk131 Requisites and Validity
25Tk134 Validity
25Tk134(6) k. Unconscionability. Most Cited Cases

When a party to an arbitration agreement argues that the agreement is unconscionable and unenforceable, that claim is decided based on the same state law principles that apply to contracts generally.

[4] Alternative Dispute Resolution 25T 113

25T Alternative Dispute Resolution
25TII Arbitration
25TII(A) Nature and Form of Proceeding
25Tk113 k. Arbitration Favored; Public Policy. Most Cited Cases

The Federal Arbitration Act (FAA) expresses a liberal federal policy favoring arbitration agreements. 9 U.S.C.A. § 1 et seq.

[5] Alternative Dispute Resolution 25T 113

25T Alternative Dispute Resolution
25TII Arbitration
25TII(A) Nature and Form of Proceeding
25Tk113 k. Arbitration Favored; Public Policy.
Most Cited Cases
New Jersey's public policy favors enforcement of valid agreements to arbitrate. N.J.S.A. 2A:24-1 et seq.

[6] Alternative Dispute Resolution 25T 134(3)

25T Alternative Dispute Resolution
25TII Arbitration
25TII(B) Agreements to Arbitrate
25Tk131 Requisites and Validity
25Tk134 Validity
25Tk134(3) k. Validity of Assent.
Most Cited Cases

Alternative Dispute Resolution 25T 134(6)

25T Alternative Dispute Resolution
25TII Arbitration
25TII(B) Agreements to Arbitrate
25Tk131 Requisites and Validity
25Tk134 Validity
25Tk134(6) k. Unconscionability.
Most Cited Cases
Generally recognized contract defenses, such as duress, fraud, and unconscionability, can justify judicial refusal to enforce an arbitration agreement.

[7] Contracts 95 1

95 Contracts
95I Requisites and Validity

95I(A) Nature and Essentials in General

95k1 k. Nature and Grounds of Contractual Obligation. Most Cited Cases

The contract defense of unconscionability calls for a fact-sensitive analysis in each case, even when a contract of adhesion is involved.

[8] Contracts 95 ⚿1

95 Contracts

95I Requisites and Validity

95I(A) Nature and Essentials in General

95k1 k. Nature and Grounds of Contractual Obligation. Most Cited Cases

In determining whether to enforce the terms of a contract of adhesion, the court looks not only to the take-it-or-leave-it nature or the standardized form of the document, but also to: (1) the subject matter of the contract; (2) the parties' relative bargaining positions; (3) the degree of economic compulsion motivating the "adhering" party; and (4) the public interests affected by the contract.

[9] Contracts 95 ⚿1

95 Contracts

95I Requisites and Validity

95I(A) Nature and Essentials in General

95k1 k. Nature and Grounds of Contractual Obligation. Most Cited Cases

The *Rudbart* factors for determining whether to enforce the terms of a contract of adhesion focus on the procedural and substantive aspects of a contract of adhesion in order to determine whether the contract is so oppressive or inconsistent with the vindication of public policy that it would be unconscionable to permit its enforcement.

[10] Contracts 95 ⚿1

95 Contracts
95I Requisites and Validity
95I(A) Nature and Essentials in General
95k1 k. Nature and Grounds of Contractual Obligation. Most Cited Cases
Courts generally apply a sliding-scale approach to determine overall unconscionability of a contract of adhesion, considering the relative levels of both procedural and substantive unconscionability.

[11] Antitrust and Trade Regulation 29T ⚿396

29T Antitrust and Trade Regulation
29TIII Statutory Unfair Trade Practices and Consumer Protection
29TIII(E) Enforcement and Remedies
29TIII(E)7 Relief
29Tk395 Costs
29Tk396 k. In General. Most Cited Cases

Antitrust and Trade Regulation 29T ⚿397

29T Antitrust and Trade Regulation
29TIII Statutory Unfair Trade Practices and Consumer Protection
29TIII(E) Enforcement and Remedies
29TIII(E)7 Relief
29Tk395 Costs
29Tk397 k. Attorney Fees. Most Cited Cases

Consumer Credit 92B ⚿67

92B Consumer Credit
92BII Federal Regulation
92BII(C) Effect of Violation of Regulations

92Bk64 Actions for Violations
92Bk67 k. Judgment and Relief; Attorney Fees. Most Cited Cases
An award of attorney fees and costs to prevailing plaintiffs is mandatory under both the New Jersey Consumer Fraud Act (CFA) and the federal Truth in Lending Act (TILA). Truth in Lending Act, § 130(a)(3), 15 U.S.C.A. § 1640(a)(3); N.J.S.A. 56:8-19.

An award of attorney fees and costs to prevailing plaintiffs is mandatory under both the New Jersey Consumer Fraud Act (CFA) and the federal Truth in Lending Act (TILA). Truth in Lending Act, § 130(a)(3), 15 U.S.C.A. § 1640(a)(3); N.J.S.A. 56:8-19.

[12] Costs 102 ⚿194.10

102 Costs
102VIII Attorney Fees
102k194.10 k. In General. Most Cited Cases
Fee-shifting provisions can deter a litigant from pursuing a claim.

[13] Alternative Dispute Resolution 25T ⚿269

25T Alternative Dispute Resolution
25TII Arbitration
25TII(F) Arbitration Proceedings
25Tk269 k. Costs. Most Cited Cases
The public policy of New Jersey permits an arbitration agreement to shift costs and attorney fees to a consumer who brings frivolous or bad faith claims. N.J.S.A. 2A:15-59.1.

[14] Alternative Dispute Resolution 25T ⚿134(6)

25T Alternative Dispute Resolution
25TII Arbitration

25TII(B) Agreements to Arbitrate
25Tk131 Requisites and Validity
25Tk134 Validity
25Tk134(6) k. Unconscionability. Most Cited Cases

Question of unconscionability of cost-shifting provision in arbitration clause of mortgage loan contract between consumer and sub-prime mortgage lender was not moot, though sub-prime mortgage lender made after-the-fact offer to pay all of consumer's arbitration costs.

[15] Alternative Dispute Resolution 25T 134(6)

25T Alternative Dispute Resolution
25TII Arbitration
25TII(B) Agreements to Arbitrate
25Tk131 Requisites and Validity
25Tk134 Validity
25Tk134(6) k. Unconscionability. Most Cited Cases

If arbitrator interpreted cost-shifting provision in arbitration clause of mortgage loan contract between consumer and sub-prime lender as giving arbitrator unfettered discretion to shift entire cost of arbitration to consumer in an arbitration in which consumer asserted affirmative statutory claims, the cost-shifting provision would be unconscionable; risk to consumer that she would be required to pay all arbitration costs created substantial and unreasonable deterrent to vindication of her statutory rights and those of others similarly situated.

[16] Alternative Dispute Resolution 25T 134(6)

25T Alternative Dispute Resolution
25TII Arbitration
25TII(B) Agreements to Arbitrate
25Tk131 Requisites and Validity

25Tk134 Validity
25Tk134(6) k. Unconscionability.
Most Cited Cases
Cost-shifting provision in arbitration clause of mortgage loan contract between consumer and sub-prime lender would be unconscionable, if interpreted by arbitrator as giving arbitrator unfettered discretion to shift entire cost of arbitration to consumer in an arbitration in which consumer asserted affirmative statutory claims, though agreement stated that lender would consider, in good faith, advancing costs to consumer; such an advance would merely be a loan, and thus, there was still be a risk to consumer that she would be required to pay all arbitration costs, which risk created substantial and unreasonable deterrent to vindication of her statutory rights and those of others similarly situated.

[17] Alternative Dispute Resolution 25T 151

25T Alternative Dispute Resolution
25TII Arbitration
25TII(B) Agreements to Arbitrate
25Tk150 Operation and Effect
25Tk151 k. In General. Most Cited Cases
By agreeing to arbitrate a statutory claim, a party does not forgo the substantive rights afforded by the statute; the party only submits to their resolution in an arbitral rather than a judicial, forum.

[18] Antitrust and Trade Regulation 29T 396

29T Antitrust and Trade Regulation
29TIII Statutory Unfair Trade Practices and Consumer Protection
29TIII(E) Enforcement and Remedies
29TIII(E)7 Relief
29Tk395 Costs
29Tk396 k. In General. Most Cited Cases

Antitrust and Trade Regulation 29T 397

29T Antitrust and Trade Regulation
29TIII Statutory Unfair Trade Practices and Consumer Protection
29TIII(E) Enforcement and Remedies
29TIII(E)7 Relief
29Tk395 Costs
29Tk397 k. Attorney Fees. Most Cited Cases
Just as defendants may not enforce exculpatory waivers that seek a release from a statutorily imposed duty, defendants may not limit a consumer's ability to pursue the statutory remedy of attorney fees and costs when it is available to prevailing parties.

[19] Alternative Dispute Resolution 25T 134(6)

25T Alternative Dispute Resolution
25TII Arbitration
25TII(B) Agreements to Arbitrate
25Tk131 Requisites and Validity
25Tk134 Validity
25Tk134(6) k. Unconscionability. Most Cited Cases
If arbitrator interpreted attorney fee provision in arbitration clause of mortgage loan contract between consumer and sub-prime lender, which stated that unless inconsistent with applicable law each party would bear the expense of that party's attorney fees regardless of which party prevailed in arbitration, as preventing arbitrator from awarding statutory attorney fees to consumer when that statutory remedy was merely discretionary, the attorney fee provision would be unconscionable.

[20] Alternative Dispute Resolution 25T 134(6)

25T Alternative Dispute Resolution
25TII Arbitration
25TII(B) Agreements to Arbitrate
25Tk131 Requisites and Validity
25Tk134 Validity
25Tk134(6) k. Unconscionability.
Most Cited Cases
If arbitrator interpreted appellate cost provision in arbitration clause of mortgage loan contract between consumer and sub-prime lender, which stated that in an appeal of a single arbitrator's decision to panel of three arbitrators the appellant would bear the costs of appeal regardless of the outcome, as requiring consumer, as prevailing-party appellant, to incur entire costs of arbitration appeal, the appellate cost provision would be unconscionable.

[21] Alternative Dispute Resolution 25T 134(6)

25T Alternative Dispute Resolution
25TII Arbitration
25TII(B) Agreements to Arbitrate
25Tk131 Requisites and Validity
25Tk134 Validity
25Tk134(6) k. Unconscionability.
Most Cited Cases
Class-arbitration waiver, in arbitration clause of mortgage loan contract between consumer and sub-prime lender, was not unconscionable; consumer had adequate incentive to bring her claims, under federal Truth in Lending Act (TILA), federal Real Estate Settlement Procedures Act (RESPA), and New Jersey Consumer Fraud Act (CFA), as an individual action because her damages were substantial and foreclosure of her home was at stake, and the statutes under which consumer sought relief provided for attorney fees and costs to prevailing plaintiffs. Real Estate Settlement Procedures

Act of 1974, § 2 et seq., 12 U.S.C.A. § 2601 et seq.; Truth in Lending Act, § 102, 15 U.S.C.A. § 1601; N.J.S.A. 56:8-1 et seq.

[22] Alternative Dispute Resolution 25T 134(6)

25T Alternative Dispute Resolution
25TII Arbitration
25TII(B) Agreements to Arbitrate
25Tk131 Requisites and Validity
25Tk134 Validity
25Tk134(6) k. Unconscionability. Most Cited Cases

Under New Jersey law, a class-arbitration waiver in an arbitration agreement is not unconscionable per se.

[23] Alternative Dispute Resolution 25T 134(6)

25T Alternative Dispute Resolution
25TII Arbitration
25TII(B) Agreements to Arbitrate
25Tk131 Requisites and Validity
25Tk134 Validity
25Tk134(6) k. Unconscionability. Most Cited Cases

Arbitration clause of mortgage loan contract between consumer and sub-prime lender, which excluded foreclosure actions from arbitration, was not unconscionable, though mortgagor would be required to arbitrate statutory claims against mortgagee that were substantively similar to counterclaims that mortgagor brought against mortgagee in foreclosure action, and it was burdensome to litigate similar claims in different forums.

[24] Antitrust and Trade Regulation 29T ⚿396

29T Antitrust and Trade Regulation
29TIII Statutory Unfair Trade Practices and Consumer Protection
29TIII(E) Enforcement and Remedies
29TIII(E)7 Relief
29Tk395 Costs
29Tk396 k. In General. Most Cited Cases

Antitrust and Trade Regulation 29T ⚿397

29T Antitrust and Trade Regulation
29TIII Statutory Unfair Trade Practices and Consumer Protection
29TIII(E) Enforcement and Remedies
29TIII(E)7 Relief
29Tk395 Costs
29Tk397 k. Attorney Fees. Most Cited Cases
For purposes of eligibility for payment of reasonable attorneys fees and costs, the Consumer Fraud Act (CFA) makes no distinction between a person who raises the Act's provisions in an affirmative claim and one who pleads it as a defense. N.J.S.A. 56:8-19.

[25] Alternative Dispute Resolution 25T ⚿134(6)

25T Alternative Dispute Resolution
25TII Arbitration
25TII(B) Agreements to Arbitrate
25Tk131 Requisites and Validity
25Tk134 Validity
25Tk134(6) k. Unconscionability.
Most Cited Cases
It is not unconscionable to require that the proceedings before the arbitrator be kept confidential, when the arbitrator's written award is not required to be kept

confidential.

On certification of a Question of Law to United States Circuit Court of Appeals for the Third Circuit.

Madeline L. Houston argued the cause for appellant (Houston & Totaro, attorneys).
Martin C. Bryce, Jr. argued the cause for respondent (Ballard Spahr Andrews & Ingersoll, attorneys).
Baher Z. Azmy argued the cause for amici curiae American Civil Liberties Union of New Jersey, The New Jersey Institute for Social Justice, New Jersey Citizen Action, The New Jersey Public Policy Research Institute, The National Association of Consumer Advocates, AARP, The Center for Responsible Lending, and Seton Hall School of Law Center for Social Justice (Mr. Azmy, Seton Hall University School of Law Center for Social Justice Civil Litigation Clinic, attorney; Mr. Azmy and Jessica Yager, Joseph Faulkner and Melissa Kelly, on the brief).
Henry P. Wolfe argued the cause for amicus curiae Legal Services of New Jersey (Melville D. Miller, Jr., President, attorney; Mr. Wolfe, Mr. Miller, David G. McMillin, Marcia E. Suarez, Marcie B. Harrison, Kristin A. Mateo, Carrie Ferraro and Dawn K. Miller, on the brief).
Jeffrey C. Burstein, Assistant Attorney General, argued the cause for amici curiae Attorney General of New Jersey and The New Jersey Division of Consumer Affairs (Zulima V. Farber, Attorney General, attorney; Mr. Burstein and Carol G. Jacobson, on the brief).
David M. Gossett, a member of the Illinois and District of Columbia bars, argued the cause for amicus curiae Chamber of Commerce of the United States of America (Drinker Biddle & Reath, attorneys; Mr. Gossett, Evan M. Tager, a member of the New York and District of Columbia bars, Robin S. Conrad, a member of the District of Columbia bar, Amar D. Sarwal, a member of the District of Columbia bar,

of counsel; Andrew B. Joseph, on the brief).
Mark L. Rienzi, Christopher Lipsett, a member of District of Columbia and New York bars, Eric J. Mogilnicki, a member of District of Columbia and Massachusetts bars and Kelly Thompson Cochran, a member of the District of Columbia and Virginia bars, submitted a brief on behalf of amicus curiae American Financial Services Association (Mr. Rienzi, attorney).
Marvin J. Brauth and Jeffrey J. Brookner submitted a brief on behalf of amicus curiae New Jersey Business and Industry Association (Wilentz, Goldman & Spitzer, attorneys; Mr. Brauth, of counsel; Mr. Brauth and Mr. Brookner, on the brief).*Madeline L. Houston* argued the cause for appellant (*Houston & Totaro,* attorneys).*Martin C. Bryce, Jr.* argued the cause for respondent (*Ballard Spahr Andrews & Ingersoll,* attorneys).*Baher Z. Azmy* argued the cause for *amici curiae* American Civil Liberties Union of New Jersey, The New Jersey Institute for Social Justice, New Jersey Citizen Action, The New Jersey Public Policy Research Institute, The National Association of Consumer Advocates, AARP, The Center for Responsible Lending, and Seton Hall School of Law Center for Social Justice (*Mr. Azmy,* Seton Hall University School of Law Center for Social Justice Civil Litigation Clinic, attorney; *Mr. Azmy* and *Jessica Yager, Joseph Faulkner* and *Melissa Kelly,* on the brief).*Henry P. Wolfe* argued the cause for *amicus curiae* Legal Services of New Jersey (*Melville D. Miller, Jr.,* President, attorney; *Mr. Wolfe, Mr. Miller, David G. McMillin, Marcia E. Suarez, Marcie B. Harrison, Kristin A. Mateo, Carrie Ferraro* and *Dawn K. Miller,* on the brief).*Jeffrey C. Burstein,* Assistant Attorney General, argued the cause for *amici curiae* Attorney General of New Jersey and The New Jersey Division of Consumer Affairs (*Zulima V. Farber,* Attorney General, attorney; *Mr. Burstein* and *Carol G. Jacobson,* on the brief).*David M. Gossett,* a member of the Illinois and District of Columbia bars, argued the cause for *amicus curiae* Chamber of Commerce of the

United States of America (*Drinker Biddle & Reath,* attorneys; *Mr. Gossett,* *Evan M. Tager,* a member of the New York and District of Columbia bars, *Robin S. Conrad,* a member of the District of Columbia bar, *Amar D. Sarwal,* a member of the District of Columbia bar, of counsel; *Andrew B. Joseph,* on the brief).*Mark L. Rienzi, Christopher Lipsett,* a member of District of Columbia and New York bars, *Eric J. Mogilnicki,* a member of District of Columbia and Massachusetts bars and *Kelly Thompson Cochran,* a member of the District of Columbia and Virginia bars, submitted a brief on behalf of *amicus curiae* American Financial Services Association (*Mr.Rienzi,* attorney).*Marvin J. Brauth* and *Jeffrey J. Brookner* submitted a brief on behalf of *amicus curiae* New Jersey Business and Industry Association (*Wilentz, Goldman & Spitzer,* attorneys; *Mr. Brauth,* of counsel; *Mr. Brauth* and *Mr. Brookner,* on the brief).

Justice LaVECCHIA delivered the opinion of the Court.

***1** This matter presents a question of law certified and submitted by the United States Court of Appeals for the Third Circuit pursuant to the procedures set forth in *Rule* 2:12A. We have been asked whether an arbitration agreement found in a consumer loan contract is unconscionable, in whole or in part, under New Jersey contract law. Because many of the agreement's provisions are ambiguous, interpretation of the contract by an arbitrator is necessary before there can be a final resolution of this dispute. However, to the extent that the procedural posture of this matter permits, we hold that several parts of the arbitration agreement may be unenforceable based on unconscionability doctrine if interpreted by an arbitrator unfavorably to the consumer as described herein.

I.

[1] We begin with the facts as presented by the federal court, although we acknowledge the presence of factual disputes

between the parties. *R.* 2:12A-4. The purpose of the certification process is to answer the question of law submitted pursuant to *Rule* 2:12A, not to resolve those factual differences. *See R.* 2:12A-1.

Plaintiff Delta Funding Corp. (Delta) is a New York mortgage lender that extends loans primarily to borrowers in the sub-prime lending market. In December 1999, Delta entered into a mortgage loan contract with defendant Alberta Harris, a seventy-eight-year-old woman with only a sixth-grade education and little financial sophistication. The $37,700 loan was secured by a mortgage on Harris's home in Newark.[FN1] The loan had an annual percentage rate of fourteen percent. At the time, Harris owned her home outright and had lived in it for more than thirty years. Delta subsequently assigned the loan to Wells Fargo as trustee.

The loan contains an arbitration agreement that allows either party to elect binding arbitration as the forum to resolve covered claims. The agreement excludes from arbitration "any action to effect a judicial or non-judicial foreclosure or to establish a deficiency judgment," as well as a number of similar actions. The agreement provides that "[t]here shall be no right or authority for any Claims to be arbitrated on a class action or class-wide basis." In respect of costs, the agreement further provides that

[a]t your written request, we will consider in good faith making a temporary advance of all or part of the filing, administrative and/or hearing fees in connection with any Claim you initiate as to which you or we seek arbitration. At the conclusion of the arbitration, the arbitrator will decide who will ultimately be responsible for paying the filing, administrative and/or hearing fees in connection with the arbitration. Unless inconsistent with applicable law, each party shall bear the expense of that party's attorneys', experts' and witness fees, regardless of which party prevails in the arbitration.

The agreement also provides for an appeal procedure within arbitration and states that "[t]he costs of ... [any such] appeal will be borne by the appealing party regardless of the outcome of the appeal."

*2 Under the agreement, Harris is permitted to select the American Arbitration Association (AAA), J.A.M.S./Endispute (JAMS), or the National Arbitration Forum (NAF) as the forum for any claim. The agreement also contains a severability clause, which states that "[i]f any portion of this Agreement is deemed invalid or unenforceable under any law or statute consistent with the [Federal Arbitration Act], it shall not invalidate the remaining portions of this Agreement or the Credit Transaction, each of which shall be enforceable regardless of such invalidity."

When Harris, whose only source of income was Social Security payments, was unable to make the required loan payments, Wells Fargo instituted a mortgage foreclosure action in New Jersey Superior Court. Harris responded with an answer and counterclaim, as well as a third-party complaint against Delta, alleging violations of the Truth in Lending Act (TILA), 15 *U.S.C.* § § 1601 to -67, the Real Estate Settlement Procedures Act (RESPA), 12 *U.S.C.* § § 2601 to -17, and the New Jersey Consumer Fraud Act (CFA), *N.J.S.A.* 56:8-1 to -135. Thereafter, Delta filed a petition in federal district court seeking to compel arbitration of Harris's affirmative claims against Delta. Harris filed a motion for summary judgment contending that the arbitration agreement was unconscionable and unenforceable. In March 2004, the district court denied that motion for summary judgment and granted Delta's motion to compel arbitration. *Delta Funding Corp. v. Harris*, 396 *F.Supp.*2d 512 (D.N.J.2004). The state court presiding over the foreclosure action then dismissed Harris's third-party complaint against Delta, which had been held in abeyance.

Harris appealed to the United States Court of Appeals for the Third Circuit. A three-judge panel of the Third Circuit issued a petition order to this Court pursuant to *Rule* 2:12A-3, in which the panel certified the question: "Is the arbitration clause at issue in this case, or any provision thereof, unconscionable under New Jersey law, *N.J. Stat. Ann.* § 12A:2-302, and if so, should such provision or provisions be severed." *Delta Funding Corp. v. Harris,* No. 04-1951, 2005 *U.S.App. LEXIS* 24531 (3d Cir. July 27, 2005). Harris submitted a brief urging that we grant certification, but asking that we remove the reference to *N.J.S.A.* 12A:2-302 because her unconscionability claim is based on the common law. *See R.* 2:12A-2.

We granted certification, reformulating the question as follows: "Is the arbitration agreement at issue, or any provision thereof, unconscionable under New Jersey law, and, if so, should such provision or provisions be severed?" 185 *N.J.* 255, 883 *A.*2d 1055 (2005). Briefs were received from the parties; in addition, numerous groups filed submissions as friends of the court. In support of Harris, amici briefs were received from Legal Services of New Jersey, the Attorney General on behalf of the New Jersey Division of Consumer Affairs, the American Civil Liberties Union of New Jersey, the New Jersey Institute for Social Justice, New Jersey Citizen Action, the New Jersey Public Policy Research Institute, the National Association of Consumer Advocates, AARP, the Center For Responsible Lending, and Seton Hall School of Law Center for Social Justice. The United States Chamber of Commerce, the New Jersey Business and Industry Association, and the American Financial Services Association filed amicus briefs in support of Delta.

II.

*3 [2] We address first the procedural posture of this matter. Because we have been asked by the Third Circuit to answer a discrete question of state law, our inquiry is limited. Under federal arbitration law, it is ordinarily the role of an arbitrator and not the courts to interpret ambiguous provisions of an arbitration agreement. *Green Tree Fin.Corp. v. Bazzle*, 539 *U.S.* 444, 451-53, 123 *S.Ct.* 2402, 2407, 156 *L. Ed.*2d 414, 422-23 (2003) (plurality opinion); *PacifiCare Health Sys., Inc. v. Book*, 538 *U.S.* 401, 406-07, 123 *S.Ct.* 1531, 1535-36, 155 *L. Ed.*2d 578, 584 (2003). That general rule is especially applicable where the arbitration agreement contains "sweeping language concerning the scope of the questions committed to arbitration." *Bazzle, supra*, 539 *U.S.* at 453, 123 *S.Ct.* at 2407, 156 *L. Ed.*2d at 4223. Most of the disputed provisions in the instant arbitration agreement are, to some degree, ambiguous. To the extent that the unconscionability of those provisions ultimately turns on how the arbitrator resolves the ambiguities, we are unable to determine whether the provisions are, in fact, unconscionable. [FN2] For purposes of answering the question of state law posed by the Third Circuit, we address how the ambiguous provisions, if interpreted and applied in a manner detrimental to Harris, could be unconscionable. In doing so, we identify general principles of New Jersey contract law that the Third Circuit and the arbitrator can then apply to the agreement.

III.

[3][4][5][6] In today's companion decision, *Muhammad v. County Bank of Rehoboth Beach*, --- *N.J.* ---- (2006) (slip op. at ----), we recognized the basic premise that when a party to an arbitration agreement argues that the agreement is unconscionable and unenforceable, that claim is decided based on the same state law principles that apply to contracts

generally. The Federal Arbitration Act (FAA), 9 *U.S.C.* § § 1 to -16, expresses a "liberal federal policy favoring arbitration agreements." *Moses H. Cone Mem'l Hosp. v. Mercury Constr. Corp.*, 460 *U.S.* 1, 24, 103 *S.Ct.* 927, 941, 74 *L. Ed.*2d 765, 785 (1983). New Jersey's public policy similarly favors enforcement of valid agreements to arbitrate. *See Martindale v. Sandvik, Inc.*, 173 *N.J.* 76, 83-86, 800 *A.*2d 872 (2002) (citing New Jersey's Arbitration Act, *N.J.S.A.* 2A:24-1 to -11). The FAA, however, permits courts to refuse enforcement of an arbitration agreement to the extent "such grounds ... exist at law or in equity for the revocation of any contract." 9 *U.S.C.* § 2. Generally recognized contract defenses, such as duress, fraud, and unconscionability, can justify judicial refusal to enforce an arbitration agreement. *Doctor's Assocs., Inc. v. Casarotto*, 517 U.S. 681, 686-87, 116 *S.Ct.* 1652, 1656, 134 *L. Ed.*2d 902, 908-09 (1996); *Muhammad, supra*, --- *N.J.* at ---- (slip op. at ----); *Martindale, supra*, 173 *N.J.* at 85-86, 800 *A.*2d 872.

***4** [7][8] The defense of unconscionability, specifically, calls for a fact-sensitive analysis in each case, even when a contract of adhesion is involved. *Muhammad, supra*, --- *N.J.* at ---- (slip op. at ----). This Court has recognized that contracts of adhesion necessarily involve indicia of procedural unconscionability. *Id.* at ---- (slip op. at ----). We have identified, therefore, four factors as deserving of attention when a court is asked to declare a contract of adhesion unenforceable. *Rudbart v. n.Jersey Dist. Water Supply Comm'n*, 127 *N.J.* 344, 356, 605 *A.*2d 681, *cert. denied*, 506 *U.S.* 871, 113 *S.Ct.* 203, 121 *L. Ed.*2d 145 (1992).

[I]n determining whether to enforce the terms of a contract of adhesion, [we] look[ ] not only to the take-it-or-leave-it nature or the standardized form of the document but also to [(1)] the subject matter of the contract, [(2)] the parties' relative bargaining positions, [(3)] the degree of economic compulsion motivating the "adhering" party, and [(4)] the

public interests affected by the contract.
[*Ibid.*]

[9][10] The *Rudbart* factors focus on the procedural and substantive aspects of a contract of adhesion in order to determine whether the contract is so oppressive, *Martindale, supra,* 173 *N.J.* at 90, 800 *A.*2d 872, or inconsistent with the vindication of public policy, *Muhammad, supra,* ---*N.J.* at ---- (slip op. at ----), that it would be unconscionable to permit its enforcement. Courts generally have applied a sliding-scale approach to determine overall unconscionability, considering the relative levels of both procedural and substantive unconscionability. *See Sitogum Holdings, Inc. v. Ropes,* 352 *N.J.Super.* 555, 565-66, 800 *A.*2d 915 (Ch.Div.2002); *see also Muhammad, supra,* --- *N.J.* at ---- n. 2 (slip op. at 13 n. 2) (noting appropriateness of sliding-scale analysis for contracts of adhesion).

In this matter, Harris alleges certain facts surrounding her signing of the contract that suggest a high level of procedural unconscionability. We do not resolve those disputed facts, nor do we rely on them in deciding the unconscionability question before us. It is sufficient to note that the arbitration agreement is in a consumer contract of adhesion where Delta, as a financial institution, possessed superior bargaining power and was the more sophisticated party in the transaction. *Delta Funding Corp., supra,* 396 *F.Supp.*2d at 516. Although that level of procedural unconscionability does not, by itself, render the arbitration agreement unenforceable, it must be taken into account as we turn to the "public interests affected by the contract." *Rudbart, supra,* 127 *N.J.* at 356, 605 *A.*2d 681.

IV.

In addition to Harris's broad assertion that the arbitration agreement as a whole is unconscionable and unenforceable, an argument that we find unpersuasive for reasons explained *infra*, several discrete provisions of the agreement are alleged to raise unconscionability concerns because they have the effect of limiting the substantive statutory rights and remedies available to a consumer. Related to that assertion is the claim that it is unconscionable for an arbitration agreement to include a "cost-shifting" provision that allows an arbitrator unfettered discretion to allocate the entire cost of arbitration to a consumer. Because we find that the provisions relevant to those claims can be applied in a manner that is unconscionable and unenforceable under New Jersey law, we address them first in responding to the Third Circuit's inquiry.

A. Hearing-level costs

***5** [11] The arbitration agreement states that "[a]t the conclusion of the arbitration, the arbitrator will decide who will ultimately be responsible for paying the filing, administrative and/or hearing fees in connection with the arbitration." It is beyond dispute that Harris would be entitled to costs if she prevailed on her CFA or TILA claims. An award of attorney's fees and costs to prevailing plaintiffs is mandatory under both statutes. *N.J.S.A.* 56:8-19; 15 *U.S.C.* § 1640(a)(3). If, however, Harris did not prevail in arbitration (or if she prevailed only on her RESPA claim and the arbitrator declined to make a discretionary award of costs as allowed under RESPA, 12 *U.S.C.* § 2607(d)(5)), then Harris could be forced to bear the entire cost of the arbitration.[FN3]

[12] It is well understood that fee-shifting provisions can deter a litigant from pursuing a claim. *See Dare v. Freefall Adventures, Inc.*, 349 *N.J.Super.* 205, 221-24, 793 *A.*2d 125 (App.Div.) (refusing to enforce mandatory fee-shifting provision against a recreational sports participant), *certif. denied*, 174 *N.J.* 43, 803 *A.*2d 638 (2002); *N .J. Coal. of Health Care Prof'ls, Inc. v. N.J. Dep't of Banking and Ins., Div. of Ins.*, 323 *N.J.Super.* 207, 263, 732 *A.*2d 1063 (App.Div.) (noting that "imposing counsel fees in favor of an insurance company may chill resort to the dispute resolution process"), *certif. denied*, 162 *N.J.* 485, 744 *A.*2d 1208 (1999). The prospect of having to shoulder all the costs of arbitration could chill Harris and similarly situated consumers from pursuing their statutory claims through mandatory arbitration.[FN4] Other courts that have analyzed the allocation of arbitration costs under federal law, have taken into consideration the possible " 'chilling effect' " that certain cost provisions can have both on an individual claimant and on similarly situated litigants. *Morrison v. Circuit City Stores, Inc. ..* 317 *F.*3d 646, 657-67 (6th Cir.2003) (finding cost-splitting provision unenforceable); *see also Scovill v. WSYX/ABC, Sinclair Broad. Group, Inc.*, 425 *F.*3d 1012, 1019-21 (6th Cir.2005) (finding cost-shifting provision unenforceable under *Morrison*).

[13][14][15][16] Although the public policy of our State would permit an arbitration agreement to shift costs and attorney's fees to a consumer who brings "frivolous" or "bad faith" claims, *see N.J .S.A.* 2A:15-59.1 (recognizing public policy against frivolous and bad faith litigation and establishing penalties for same), no such limitation is evident in the cost-shifting provision applicable to Harris. Delta claims that arbitrators rarely, if ever, shift costs to a consumer. However, contract unconscionability must be decided based on the contract as written because the language of the agreement is what consumers must consider when assessing whether to pursue a statutory-rights claim

against Delta.[FN5] Delta drafted the arbitration agreement giving the arbitrator unfettered discretion to shift the entire cost of arbitration to Harris. The agreement as written, and as yet uninterpreted by an arbitrator, could force Harris to bear the risk that she will be required to pay all arbitration costs. That risk is unconscionable in that it is a deterrent to the vindication of her statutory rights.

***6** The fact that, under the agreement's terms, Delta will consider, in "good faith," advancing any costs to Harris does not alter our analysis. Even if Delta elected to advance the costs of the arbitration to Harris, the advance is merely a loan. Harris ultimately could still be saddled with the entire cost of arbitration. That creates a substantial and unreasonable deterrent to the vindication of the statutory rights of Harris and others who are similarly situated. A contract of adhesion that contains such a term, which effectively would deter the vindication of a consumer's statutory rights, would be unconscionable and unenforceable if interpreted and applied in the manner described above.

B. Attorney's fees

[17][18] Harris's arbitration agreement states that "[u]nless inconsistent with applicable law, each party shall bear the expense of that party's attorneys', experts' and witness fees, regardless of which party prevails in the arbitration." " '[B]y agreeing to arbitrate a statutory claim, a party does not forgo the substantive rights afforded by the statute; it only submits to their resolution in an arbitral rather than a judicial, forum.' " *Martindale, supra*, 173 *N.J.* at 93, 800 *A.*2d 872 (quoting *Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc.*, 473 *U.S.* 614, 628, 105 *S.Ct.* 3346, 3354, 87 *L. Ed.*2d 444, 456 (1985)). Although this requirement has its genesis in federal arbitration law, it is equally applicable in determining unconscionability under New Jersey law. Just as defendants

may not enforce exculpatory waivers that seek a release from a statutorily imposed duty, *McCarthy v. NASCAR, Inc.*, 48 *N.J.* 539, 543, 226 *A.*2d 713 (1967), defendants may not limit a consumer's ability to pursue the statutory remedy of attorney's fees and costs when it is available to prevailing parties. *See Muhammad, supra,* --- *N.J.* at ---- (slip op. at ----) (finding class-arbitration bar that effectively acts as exculpatory waiver unconscionable).

[19] The CFA and TILA provide mandatory attorney's fees and costs to prevailing parties. Plainly, those remedies are recoverable under Harris's arbitration agreement. On the other hand, under RESPA whether a prevailing party will be awarded attorney's fees and costs is discretionary. The arbitration agreement's clause that requires parties to bear their own fees and costs, no matter who prevails, "[u]nless inconsistent with applicable law," suggests that the arbitrator may not have the power to award attorney's fees when that statutory remedy is merely discretionary.[FN6] The possibility of an award of fees to a prevailing party serves to encourage pursuit of RESPA's protections. To the extent that this provision in Harris's consumer contract would prevent her from recovering discretionary attorney's fees and costs under RESPA, it is unconscionable.

C. Appeal costs

[20] The arbitration agreement states that
if the amount in controversy exceeds $50,000, any party can appeal the award to a three-arbitrator panel administered by the same arbitration administrator which shall reconsider *de novo* any aspect of the initial award requested by the appealing party.... *The costs of such an appeal will be borne by the appealing party regardless of the outcome of the appeal.*
*7 [(Emphasis added).]

Like the attorney's fees provision discussed above, the appeals provision is unconscionable to the extent that it would bar Harris from being awarded costs if she prevailed on her appeal.[EN7] If Harris appeals and loses, she has no statutory entitlement to the remedy of costs. As such, the fact that the appeals provision requires her to bear her costs in that circumstance does not abridge Harris's substantive statutory remedies. To the extent that Harris would be required to incur the entire costs of taking an appeal, however, the appeals provision would be unconscionable. The same conclusion in respect of the unconscionability of the hearing-level costs provision applies to the allocation of costs related to appeals available within the arbitral forum.

D. Post-interpretation by arbitrator

As noted, the arbitration provisions are subject to interpretation, but only by an arbitrator. Once that occurs, if the agreement is held to permit the shifting of arbitration costs to Harris, then the unconscionable cost-shifting provision must be severed from the agreement. In that eventuality, Delta, which previously offered to pay all of Harris's arbitration costs, would be responsible for the entire costs of arbitration. *Cf. Jones v. Household Realty Corp.*, No. C-3-03-280, 2003 *U.S. Dist. LEXIS* 25882 (S.D.Ohio Dec.17, 2003) (slip op. at *16-18) (finding cost-splitting provision to be unconscionable and severing offending provision). In *Jones,* the court similarly ordered the defendant to pay "the entire cost of arbitration" based, in part, on the defendant's stipulated offer to pay such costs. *Id.* at *17. Because a severance of the potentially cost-shifting provision from Harris's agreement will not result in a cost-splitting arrangement, we need not address whether a cost-splitting arrangement would be unconscionable. We do, however, note the concerns that courts have expressed over

cost-splitting arrangements. *See* Morrison, *supra*, 317 F.3d at 657-67.

That said, if an arbitrator were to interpret all of the disputed provisions in a manner that would render them unconscionable, we have no doubt that those provisions could be severed and that the remainder of the arbitration agreement would be capable of enforcement. The arbitration agreement's broad severability clause supports that result.

V.

Harris advances several other arguments in support of her claim of unconscionability. We dispense with those arguments, beginning with her criticism of the class-arbitration waiver, and then addressing her broad-based challenges that are, in our view, essentially attacks on the general nature of arbitration.

A.

[21][22] In respect of the arbitration agreement's class-arbitration waiver, we note initially that Harris is not even seeking to bring a class claim. Furthermore, under New Jersey law, the class-arbitration waiver in her arbitration agreement is not unconscionable per se. In *Muhammad, supra,* we found a class-arbitration waiver unconscionable in the context of low-value consumer claims. --- N.J. at ---- (slip op. at). *Muhammad* is distinguishable from the instant case, as Harris is seeking more than $100,000 in damages, and it is unclear whether that includes application of statutory multipliers. The plaintiff's potential damages in *Muhammad, supra,* including statutory damage multipliers, totaled less than $600 in a complicated matter. --- *N.J.* at ---- (slip op. at ----). Harris's claim is not the type of low-value

suit that would not be litigated absent the availability of a class proceeding. Harris has adequate incentive to bring her claim as an individual action. Not only are her damages substantial, but the fact that her home is at stake in the foreclosure proceeding makes it likely that she would contact an attorney. The same cannot be said of low-value claims where individuals have little, if any, incentive to seek out an attorney. Moreover, all of the statutes under which Harris seeks relief provide for attorney's fees and costs to prevailing plaintiffs. Those remedies, in combination with the substantial damages that Harris seeks, render the class-arbitration waiver enforceable in the context of this litigation. *See Muhammad, supra,* --- *N.J.* at ---- n. 5 (slip op. at ----) (directing courts to consider the availability of attorney's fees when "substantial damages" are at stake).

B.

***8** [23] The arbitration agreement excludes any foreclosure actions that may be brought against Harris. Thus, foreclosure must proceed in court pursuant to the arbitration agreement. Indeed, that is hardly surprising in that the foreclosure of mortgages is a uniquely judicial process. "The broad statutory framework set forth in *N.J.S.A.* 2A:50-1 to -68, establishes the basis for foreclosure of mortgages." *Highland Lakes Country Club & Cmty. Ass'n v. Franzino,* 186 *N.J.* 99, 106 n. 2, 892 *A.*2d 646 (2006); *see also R.* 4:64-1 to -8 (establishing rules specific to foreclosure proceedings including *R.* 4:64-5's limitation on joinder of claims in foreclosure). Although Harris is able to raise potential defenses against Wells Fargo, the foreclosing party, in the foreclosure proceeding, as a result of the arbitration agreement she is forced to bring her third-party counterclaims against Delta in arbitration. Harris's defenses to the foreclosure action track her affirmative claims against Delta; thus, she is forced to litigate those substantively

similar claims in two different forums. That result is burdensome; however, it is not unconscionable.[FN8]

Other courts that have found similar provisions not unconscionable have noted the unique nature of the judicial remedies of foreclosure and similar actions. *See* *Walther v. Sovereign Bank*, 386 *Md.* 412, 872 *A.*2d 735, 749 (Md.2005) (stating that "foreclosure proceedings ... do not act solely to protect the interests of the mortgage lender against a defaulting debtor but instead provide protections for both sides."); *see also* *Conseco Fin.Servicing Corp. v. Wilder*, 47 *S.W.*3d 335, 343 (Ky.Ct.App.2001) (stating that claims involving security interests "have come to be heavily regulated by statute, allowing for streamlined procedures and effective protections for both sides.") (footnote omitted); *Lackey v. Green Tree Fin.Corp.*, 330 *S.C.* 388, 498 *S.E.*2d 898, 905 (S.C.Ct.App.1998) (stating that "[j]udicial remedies for the recovery of property, such as the replevin action, and the foreclosure action, provide specific procedures for protection of collateral and the parties during the pendency of the proceedings. These protections relate to both parties, and are facilitated by the enforcement procedures specified in the law.") (footnote omitted). We acknowledge that contrary determinations have been reached by other courts. *See, e.g.*, *Taylor v. Butler*, 142 *S.W* .3d 277, 284-87 (Tenn.2004), *cert. denied*, 543 *U.S.* 1147, 125 *S.Ct.* 1304, 161 *L. Ed.*2d 108 (2005); *Wis. Auto Title Loans, Inc. v. Jones*, 714 *N.W.*2d 155, 171-74 (Wis.2006).

[24] Harris's burden of having to litigate in two forums is alleviated by the fact that attorney's fees and costs are available to Harris under the CFA if she successfully asserts CFA-based defenses in the foreclosure action. As the district court observed, the Appellate Division has stated that "for the purposes of eligibility for payment of reasonable attorneys' fees and costs, the [CFA] makes no distinction between a person who raises the Act's provisions in an

affirmative claim and one who pleads it as a defense," *BJM Insulation & Constr., Inc.*, 287 *N.J.Super.* 513, 516, 671 *A.*2d 603 (App.Div.1996). Although we do not address whether attorney's fees and costs would be available in all contexts where the CFA is raised as a defense, we find the Appellate Division's analysis relevant here. Because of the arbitration clause, Harris is compelled to litigate essentially identical CFA claims in court and in arbitration. In that circumstance, Harris should, under *N.J.S.A.* 56:8-19, be eligible for attorney's fees and costs related to the foreclosure proceeding if she successfully asserts defenses based on the CFA in that proceeding.

C.

***9** Finally, we note Harris's argument that other clauses of the arbitration agreement are unconscionable, specifically the discovery and confidentiality provisions. She also contends that it is unconscionable for an arbitration agreement not to require a record of the proceedings or a reasoned and publicly available award. These claims are, at their core, a form of generalized attack on arbitration as a method of dispute resolution. As such, they are not persuasive.

Briefly, it is noteworthy that neither the arbitration agreement,[FN9] nor the rules of the potential arbitration administrators, prevent Harris from obtaining a record of the proceeding or a reasoned award. Both a written award and a record of the proceedings may be obtained upon request of one of the parties. Under the rules of the various administrators, the party seeking the written award or record may be required to pay for such request. Under our approach to costs outlined above, a question may arise as to the continued viability of the cost provisions related to written-award or record requests as applied against litigants such as Harris. Because it is unclear how the arbitrator will

ultimately interpret the broad cost allocation provisions of the arbitration agreement, we need not address any specific cost provisions set out in the rules of various arbitration administrators at this time.

[25] Finally, there is nothing in either the arbitration clause or the rules of the three arbitration administrators requiring that arbitration awards be kept confidential. It is not unconscionable to require that the proceedings before the arbitrator be kept confidential when the arbitrator's written award is not required to be kept confidential.

In conclusion, we add that to the extent that Harris advances other specific arguments in support of her claim of unconscionability, we reject those arguments, including her argument that the arbitration clause should be declared cumulatively unconscionable.

VI.

In describing the arbitration provisions, the Court does not express a view on how an arbitrator will interpret the provisions. We intend only to answer the certified question of law before us based on the limited record presented. Our assumptions as to possible interpretations of the disputed contract terms were necessary in order to address the unconscionability issues presented by the certified question.

Chief Justice PORITZ and Justices LONG, and WALLACE join in Justice LaVECCHIA's opinion. Justice ZAZZALI filed a separate opinion concurring in part and dissenting in part. Justice RIVERA-SOTO filed a separate dissenting opinion. Justice ALBIN did not participate.Justice ZAZZALI, concurring in part and dissenting in part.
To the extent that the majority opinion strikes down certain provisions of the arbitration agreement as unconscionable, I

concur. However, I disagree with the majority's conclusions regarding certain other provisions and would find them unconscionable. Additionally, even if I were to accept the majority's conclusions regarding the individual provisions, I nonetheless believe that the objectionable provisions cannot be severed from the agreement and that the agreement as a whole should be held cumulatively unconscionable. For those reasons, I respectfully dissent.

I.

***10** As Justice LaVecchia notes, this matter comes before the Court on a narrow question: "Is the arbitration agreement at issue, or any provision thereof, unconscionable under New Jersey law, and, if so, should such provision or provisions be severed?" 185 *N.J.* 255, 883 *A.*2d 1055 (2005). Because of our limited inquiry, the facts of the matter are neither controlling nor essential to my analysis. Nonetheless, they provide a context for the discussion, and therefore I will briefly recite them.

According to the certification of defendant Alberta Harris, at the time of the events in this matter, Harris was a seventy-eight year old widow living alone in her home in Newark. She has lived in that home for over thirty years and did not have a mortgage until she entered into the transaction that is the subject of this matter. Harris was educated only until the sixth grade, at which time she began working in Georgia cotton fields. Eventually, she moved north and worked in laundries pressing clothes and as a home health aide. She now lives on her monthly social security checks in the amount of $988. Out of that monthly payment, Harris must pay for heat, electricity, food, water, telephone service, life insurance, and any necessary house repairs. Harris only has one relative living in the State, in Toms River.

Based on its 2005 annual Form 10-K, plaintiff Delta Funding Corporation (Delta) "is a national specialty consumer finance company that originates, securitizes and sells ... non-conforming mortgage loans." According to the 10-K, Delta's loans primarily are secured by first mortgages on one- to four-family residential properties. Throughout our 24-year operating history, *we have focused on lending to individuals who generally do not satisfy the credit, documentation or other underwriting standards set by more traditional sources of mortgage credit,* including those entities that make loans in compliance with the conforming lending guidelines of Fannie Mae and Freddie Mac. We make mortgage loans to these borrowers for purposes such as debt consolidation, refinancing, education and home improvements.
[Emphasis added.]

Delta states that, during 2005, its weighted average interest rate was eight percent. Delta has enjoyed considerable success and growth in the industry. Its 10-K reports that, "[f]or the year ended December 31, 2005, we originated $3.8 billion of loans, an increase of $1.2 billion, or 46.9%, over the $2.6 billion of loans originated in the year ended December 31, 2004."

The issue in this matter arises out of a loan entered into by Harris and Delta in 1999. According to her answer, counterclaim and third-party complaint, in December 1999, Kim Stewart of The Lending Source, Ltd. (Lending Source) contacted Harris and asked her if she needed money. Harris answered yes and explained that her income consisted of her monthly social security check and that, due to her financial situation, she only could afford a limited amount each month in payments. Stewart then arranged for a representative of Universal Window Products, Inc. (Universal) to come to Harris's house. Once at the house, the representative had Harris sign a contract to install fifteen windows and a door. That contract did not stipulate a price for the work.

***11** After Harris signed the contract, a representative from Advanced Title Agency, Inc., apparently acting on behalf of Delta, came to her home at approximately 10 p.m. to have Harris sign loan papers to cover the cost of the windows and door. Harris was sick in bed but was told by the representative that the loan papers had to be signed at that time. Harris also alleges that she was rushed when signing the papers because the representative was "running late." The loan entered into by Harris was in the amount of $37,700 with an annual interest rate of around fourteen percent and was secured by a mortgage on Harris's home. According to Harris's complaint, at least $11,000 of the loan went to Universal and $4,000 went to points, fees, and closing costs. Of that $4,000, Harris avers that almost $2,000 went to Lending Source. As a result of the loan, Harris became responsible for a $444.44 monthly payment to Delta.

Delta subsequently assigned the loan to Wells Fargo Bank (Wells Fargo) as trustee and, when Harris was unable to make the necessary payments, Wells Fargo initiated foreclosure proceedings on her home by filing a complaint in the Superior Court. In response, Harris filed an answer, counterclaim, and third-party complaint, naming, among others, Delta, Lending Source, Universal, and Advanced Title Agency. Harris raised three affirmative defenses and seven counterclaims, essentially arguing that the loan was unconscionable and unenforceable because it was made with the knowledge that Harris could not repay it and with the intent of allowing the lender to obtain her house. As per the terms of the arbitration agreement, Delta filed a petition in federal district court seeking to compel arbitration of the counterclaims. Harris then moved for summary judgment dismissing Delta's petition, and Delta cross-moved to compel arbitration. The district court granted Delta's motion, concluding that the arbitration agreement was not unconscionable. On appeal, the Third Circuit Court of

Appeals asked this Court to resolve the instant question of law. 185 *N.J.* 255, 883 *A.*2d 1055 (2005).

II.

As a general matter, the arbitration agreement at issue in this case has three major components. First, the agreement sets the terms of arbitration through the "Resolution of Claims," "Hearing Location and Arbitration Costs," and "Federal Arbitration Act and Appeals" provisions. Second, through the "Excluded Claims" clause and accompanying definitions, the agreement explains that certain claims arising out of the transaction must be brought in arbitration while others must be brought in court, thereby creating a bifurcated claims structure. Third, the "No Class Actions, Etc." provision prohibits the arbitration of claims on a class action or class-wide basis. Apart from the definitions section, the only remaining provisions of the agreement are the severability clause, explaining that if one provision of the agreement is deemed unenforceable the other provisions continue in effect, and the "Important Additional Disclosures" provision, which explains that arbitration decisions are final.

***12** In reaching its decision, the majority concludes that certain clauses of the "Hearing Location and Arbitration Costs" and "Federal Arbitration Act and Appeals" provisions are unconscionable; that the agreement's creation of a bifurcated structure for litigating claims arising out of the same transaction-although "burdensome" on borrowers, *ante* at ---- (slip op. at 22, 883 A.2d 1055)-is not in and of itself unconscionable; that although class action waivers can be unconscionable under our decision in *Muhammad v. County Bank of Rehoboth Beach*, --- *N.J.* ---- (2006), the provision in this case is not unconscionable; and, finally, that the objectionable provisions of the agreement are severable and the agreement itself is not cumulatively unconscionable. As

stated, I agree with the majority in so far as it strikes down certain provisions as unconscionable. However, I also would find the provisions creating a bifurcated foreclosure structure and prohibiting class actions unconscionable. Moreover, even if I were to accept the majority's view of the individual provisions, I would nonetheless find that the objectionable provisions of the agreement cannot be severed and that, as a whole, the agreement should be held unconscionable.

III.

A.

In determining whether a contract is unconscionable, courts have focused on two factors: "(1) unfairness in the formation of the contract; and (2) excessively disproportionate terms." *Sitogum Holdings, Inc. v. Ropes*, 352 N.J.Super. 555, 564, 800 A.2d 915 (Ch.Div.2002). Those factors have been labeled "procedural" and "substantive" unconscionability. *Ibid.*

The first factor-procedural unconscionability-can include a variety of inadequacies, such as age, literacy, lack of sophistication, hidden or unduly complex contract terms, bargaining tactics, and the particular setting existing during the contract formation process. The second factor-substantive unconscionability-simply suggests the exchange of obligations so one-sided as to shock the court's conscience.

[*Id.* at 564-65, 800 A.2d 915 (citations omitted).]

Some courts have required that both factors be present for a finding of unconscionability, while other courts have found unconscionability based only on substantive unconscionability, and others still have used a "sliding scale" approach. *Id.* at 565-66, 800 A.2d 915.

As it pertains to contracts of adhesion, such as the arbitration agreement in this matter, this Court has identified four particularly relevant factors for determining unconscionability: "the subject matter of the contract, the parties' relative bargaining positions, the degree of economic compulsion motivating the 'adhering' party, and the public interests affected by the contract." *Rudbart v. N. Jersey Dist. Water Supply Comm'n*, 127 *N.J.* 344, 356, 605 *A.*2d 681, *cert. denied*, 506 *U.S.* 871, 113 *S.Ct.* 203, 121 *L. Ed.*2d 145 (1992). According to the majority, those "factors focus on the procedural and substantive aspects of a contract of adhesion in order to determine whether the contract is so oppressive or inconsistent with the vindication of public policy that it would be unconscionable to permit its enforcement." *Ante* at ---- (slip op. at 10) (internal citations omitted).

B.

***13** As the majority notes, at a minimum, "contracts of adhesion necessarily involve some indicia of one-sided procedural unconscionability in their formation generally due to unequal bargaining power." *Id.* at ---- (slip op. at 10). The circumstances under which this matter comes before the Court-on a sparse record that consists of mere allegations-preclude the Court from properly examining whether other factors such as age, literacy, lack of sophistication, unfair bargaining tactics, or the particular setting of the contract formation affect the determination of procedural unconscionability. *See Sitogum, supra*, 352 *N.J.Super.* at 564, 800 *A.*2d 915. Suffice it to note that the allegations, if proven true, including the late night visit to Harris's home and the rushed nature of her signing the documents, could have a significant effect on future unconscionability determinations, such as whether the loan agreement itself is unconscionable.

However, some considerations of procedural unconscionability are still apparent on the record before us and are relevant to two of *Rudbart's* factors, namely, the parties' relative bargaining positions and the public interests affected by the contract. In that respect, it is significant that Delta is a subprime lender that, in its own words, "focuse[s] on lending to individuals who generally do not satisfy the credit, documentation or other underwriting standards set by more traditional sources of mortgage credit, including those entities that make loans in compliance with the conforming lending guidelines of Fannie Mae and Freddie Mac." Accordingly, in considering this arbitration agreement, we should not lose sight of the context in which Delta operates.

C.

Turning to considerations of substantive unconscionability, I first disagree with the majority's holding that the excluded claims provision is not unconscionable. That provision, read in conjunction with the agreement's definitions of "Claim" and "Excluded Claims," as well as the opening paragraph of the agreement, creates a peculiar situation whereby certain claims arising out of the transaction are litigated in arbitration while other claims, arising out of the same transaction, must be litigated in court.

The agreement begins by "set[ting] forth the circumstances and procedures under which Claims (as defined below) may be arbitrated instead of litigated in court." "Claim" is then defined as

any claim, dispute or controversy between you and us (except for any Excluded Claims, as defined below) arising from or relating to the Credit Transaction or the relationships resulting from the Credit Transaction, including the validity, enforceability or scope of this Agreement, or the Credit Transaction. "Claim" includes claims of every kind and

nature, including but not limited to initial claims, counterclaims, cross-claims and third-party claims and claims based upon contract, tort, fraud and other intentional torts, constitution, statute, regulation, common law and equity. The term "Claim" is to be given the broadest possible meaning and includes, by way of example and without limitation, any claim, dispute or controversy that arises under or relates to the Truth in Lending Act, the Home Owners and Equity Protection Act and Regulation Z (including any purported election to rescind the Credit Transaction); the Equal Credit Opportunity Act and Regulation B; the Real Estate Settlement Procedures Act and Regulation X; the Fair Credit Reporting Act; the Fair Debt Collection Practices Act; state insurance, usury and lending laws; fraud or misrepresentation, including claims for failing to disclose material facts; other federal or state consumer protection statutes or regulations; any party's execution of this Agreement and/or willingness to be bound by the terms of this Agreement; or any dispute about soliciting, originating, making, closing, servicing, collecting or enforcing the Credit Transaction.

***14** However, the "Excluded Claims" provision then explains that "[n]otwithstanding the foregoing or any other term in this Agreement, Excluded Claims ... are excluded from arbitration. This means that neither you nor us can require the other to arbitrate any Excluded Claims." Those claims that are excluded are:

(a) any action to effect a judicial or non-judicial foreclosure or to establish a deficiency judgment; (b) any action arising out of unlawful detainer; (c) eviction or other summary proceeding to secure possession of real property securing the Credit Transaction; (d) any action to assert, collect, protect, realize upon or obtain possession of the collateral for the Credit Transaction in any bankruptcy proceeding; (e) any action to quiet title; (f) all rights of self-help including

peaceful occupation of real property and collection of rents, set-off and peaceful possession of personal property; (g) obtaining a deed in lieu of foreclosure; (h) obtaining provisional or ancillary remedies in connection with the foregoing; (i) Claims that you or we individually filed in court before the effective date of this Agreement; and (j) Claims advanced in any judicial class actions that have been finally certified as class actions before the effective date of this Agreement.

The agreement attempts to clarify the above by providing:For example, if we were to commence a foreclosure action against you in court, that action and any defenses asserted by you in that action would be adjudicated in court; however, if you asserted a counterclaim against us in that action which was covered by the scope of this Agreement, we would have the right to demand that the counterclaim be arbitrated (you would also have the right to arbitrate the counterclaim rather than asserting it in court).

Putting aside the question whether the above clauses are comprehensible-a debatable proposition-those provisions create a situation "so one-sided as to shock the ... conscience," *Sitogum, supra*, 352 *N.J.Super.* at 565, 800 *A.*2d 915; *see, e.g., Iberia Credit Bureau, Inc. v. Cingular Wireless LLC*, 379 *F.*3d 159, 169-70 (5th Cir.2004) (holding, under Louisiana law, that arbitration provision requiring that any claim customer is likely to bring be raised in arbitration while allowing cellular telephone provider to raise its claims against customer in court unconscionable); *Wisconsin Auto Title Loans, Inc. v. Jones*, 714 *N.W.*2d 155, 173 (Wis.2006) (analyzing similar provisions and stating that "[w]hile we appreciate that a one-sided arbitration provision may not be unconscionable under the facts of all cases, we conclude that the overly one-sidedness of the arbitration provision at issue

in the instant case renders the arbitration provision substantially unconscionable").

As the majority recognizes, the provisions are "burdensome," *ante* at ---- (slip op. at 22), because they require a borrower to litigate the foreclosure action and any claims permitted under the arbitration agreement in court while requiring certain other claims, arising out of the same transaction, to be brought in arbitration. *See Jones, supra*, 714 *N.W.*2d at 174 ("The possibility of dual forums for intertwined defenses and counterclaims imposes an unnecessary and undue burden on the borrower.... Uncontemplated inconvenience ... is a factor in deciding whether a clause is unconscionable." (citation omitted)). That leads to the incongruous result that a borrower defending against a foreclosure action will be forced to raise affirmative defenses in court but counterclaims, perhaps based on the same legal theory, in arbitration. In effect, by precluding counterclaims, the provision insulates Delta from damages in the court action. More important, the bifurcated process not only burdens the borrower but acts to substantially preclude vindication of his or her rights. Indeed, as noted, Delta seeks out customers in financial straits, who are exactly the type of individuals who would find it difficult, if not entirely impossible, to litigate their claims in one forum, to say nothing of having to litigate simultaneously in two.

***15** Finally, the majority's explanation that the provision is not unconscionable because a borrower may be able to obtain attorneys' fees if he or she successfully argues a New Jersey Consumer Fraud Act (CFA), *N.J.S.A.* 56:8-1 to -135, claim or defense is unpersuasive. The availability of attorneys' fees in this context places the proverbial cart before the horse because it does not remedy the burden of having to litigate one's rights in two forums. Rather, it provides relief to a borrower only *if* he or she proves a CFA

claim or defense. As such, a borrower must gamble that he or she will not only prevail but also prevail under a CFA claim or defense and then be awarded attorneys' fees. I cannot understand how such a series of assumptions protects a borrower. Further, although the majority is correct in noting that foreclosure actions are properly commenced in court, that fact does not give Delta the right to exclude claims that it finds unfavorable from that court action by forcing them into arbitration. Nor does it lessen the burden that such a bifurcated claims resolution structure imposes on borrowers. Ultimately, I see no reason for the majority's conclusion and would strike this provision down as unconscionable.

D.

The "No Class Actions, Etc." provision of the arbitration agreement prohibits borrowers from engaging in class actions or consolidated claims:

There shall be no right or authority for any Claims to be arbitrated on a class action or class-wide basis. There shall be no right to arbitrate a claim as a representative of others or in a private attorney general capacity. Furthermore, Claims brought by or on behalf of other borrowers may not be consolidated with or arbitrated in any arbitration proceeding that is considering your Claims unless said other borrowers are parties to the same Credit Transaction. Similarly, you may not join with other borrowers to bring Claims in the same arbitration proceeding unless all of the borrowers are parties to the same Credit Transaction.

This Court has explained the importance of class action lawsuits, stating that "[b]y permitting claimants to band together, class actions equalize adversaries and provide a procedure to remedy a wrong that might otherwise go unredressed." *In re Cadillac V8-6-4 Class Action*, 93 N.J. 412, 424, 461 A.2d 736 (1983). For example, one of the

advantages of class action lawsuits is that they allow litigants with small claims to join together to litigate an action. *Id.* at 424-25, 461 A.2d 736. In our contemporaneous decision in *Muhammad, supra,* --- *N.J.* at ---- (slip op. at 26), we held that class action waivers are not per se objectionable but nonetheless invalidated the waiver in that appeal because it prohibited the joining together of small claims, thereby depriving individuals of their "statutory rights under this State's consumer protection laws ." In the instant matter, the majority distinguishes *Muhammad* on the grounds that Harris is seeking $100,000 in damages, that she may be able to recover attorneys' fees, and that she has ample incentive to hire a lawyer in light of the fact that foreclosure proceedings have been initiated against her home.

***16** I do not disagree with the majority that the facts of this matter are distinguishable from those in *Muhammad.* Rather, I simply find that the specific facts here are irrelevant to a proper resolution of the issue. As the majority notes, Harris is not seeking to bring a class action claim. *Ante* at ---- (slip op. at 20). Therefore, as I see it, the issue is not whether the class action waiver is unconscionable in this limited situation. Instead, the question is whether the class action waiver is unconscionable in the context in which Delta concededly conducts its business, that is, Delta's business model seeks out those who are in financial difficulty. It is precisely those types of individuals who would benefit from being able to enter into class action suits and minimize the expense of litigation. Further, although Harris is seeking $100,000 in damages, one can expect that the same issue will arise in the context of smaller claims that are in greater need of the benefits of class action litigation. Accordingly, as with the excluded claims provision, I would find the arbitration agreement's class action waiver unconscionable.

IV.

Additionally, even if I were to accept the majority's conclusion that the excluded claims and class action provisions are not unconscionable, I nonetheless would find that the provisions the majority finds objectionable are not severable from the agreement and, in any event, that the arbitration agreement is so biased in favor of Delta that it is cumulatively unconscionable.

On the subject of severability, this Court has stated:
If striking the illegal portion *defeats the primary purpose of the contract, we must deem the entire contract unenforceable.* However, if the illegal portion does not defeat the central purpose of the contract, we can sever it and enforce the rest of the contract.
[*Jacob v. Norris, McLaughlin & Marcus*, 128 *N.J.* 10, 33, 607 *A.*2d 142 (1992) (emphasis added).]

Delta argues that the central purpose of the agreement is "arbitration which is both lawful and highly favored." I disagree. To maintain that the central purpose of the agreement is arbitration is to confuse the agreement's subject matter with its provisions. Indeed, the agreement does set up an arbitration proceeding. That much is obvious. However, it does so under rules and circumstances that are overwhelmingly beneficial to Delta, such as through the bifurcated foreclosure proceeding set up by the excluded claims provision. In other words, the purpose of the agreement is not merely to arbitrate claims; it is to arbitrate claims in a way that significantly advantages Delta at the expense of borrowers. In my view, the majority's striking down of various arbitration provisions is a sufficient basis for finding that the "primary purpose of the contract," *ibid.*, has been defeated, thereby compelling the conclusion that the entire agreement is unenforceable because the offending provisions cannot be severed.

***17** Further, the fact that the primary purpose of the agreement is to significantly advantage Delta at the expense of borrowers supports the conclusion that the entire agreement should be held cumulatively unconscionable. At a minimum, the majority has found that certain provisions relating to the rules of arbitration are unconscionable. Additionally, even if the excluded claims and class action waiver provisions are not unconscionable, as the majority finds, they are intended to provide a benefit to Delta at the expense of borrowers. Therefore, all three of the major components of the arbitration agreement are designed to benefit Delta. The only "advantage" to the borrower that I can find in the agreement is that it allows the borrower to choose which arbitration administrator to use. I conclude that such an arbitration agreement is "so one-sided," *Sitogum, supra*, 352 *N.J.Super.* at 565, 800 *A.*2d 915, that we should reject it in its entirety.

V.

Although I agree with the majority's conclusions regarding certain provisions of the agreement, I also would find the excluded claims and class action waiver provisions unconscionable. Additionally, I would strike down the entire arbitration agreement on the grounds that the provisions found objectionable by the majority are not severable and that the agreement is cumulatively unconscionable. In these circumstances we must be mindful that "[l]aymen cannot be expected to know how to protect their rights when dealing with practiced and carefully counseled adversaries." *Brotherhood of R.R. Trainmen v. Virginia*, 377 *U.S.* 1, 7, 84 *S.Ct.* 1113, 1117, 12 *L. Ed.*2d 89, 94 (1964).

Because I believe that this agreement exploits the individual and manipulates the process, I respectfully concur in part and dissent in part.

Justice RIVERA-SOTO, dissenting.

In this appeal we have been asked to "answer *a question of law* certified to [this Court] by the United States Court of Appeals for the Third Circuit...." *Rule* 2:12A-1 (emphasis supplied). That question, as modified, was: "Is the arbitration agreement at issue, or any provision thereof, unconscionable under New Jersey law, and, if so, should such provision or provisions be severed?" *Delta Funding Corp. v. Harris*, 185 *N.J.* 255, 883 *A.*2d 1055 (2005). Stated succinctly, the question before us is whether the arbitration agreement here is unconscionable.

The majority enjoins at the outset that "the purpose of the certification process is to answer the question of law submitted pursuant to *Rule* 2:12A, not to resolve those factual differences [between the parties]. *See R.* 2:12A-1." *Ante*, --- *N.J.* ---- (2006) (slip op. at 3). However, by proceeding to analyze whether any provision of the arbitration agreement at issue is unconscionable, the majority does not observe that injunction when it concedes that "the defense of unconscionability, specifically, calls for a fact-sensitive analysis in each case, even when a contract of adhesion is involved." *Ante*, --- *N.J.* ---- (2006) (slip op. at 9-10) (citation omitted). Instead, the majority engages in the resolution of facts in order to reach its conclusions that (1) "[t]he agreement as written, and as yet uninterpreted by an arbitrator, could force Harris to bear the risk that she will be required to pay all arbitration costs[, and that such] risk is unconscionable in that it is a deterrent to the vindication of her statutory rights[,]" *ante*, ---*N.J.* ---- (2006) (slip op. at 15); (2) "[t]o the extent that this provision [for prevailing party fee-shifting] in Harris's consumer contract of adhesion would prevent her from recovering discretionary attorney's fees and costs under [the Real Estate Settlement Procedures Act (RESPA)], it is unconscionable[,]" *ante*, --- *N.J.* ---- (2006) (slip op. at 17); and (3) "the appeals provision [requiring the appealing party to bear all appeal costs

regardless of outcome] is unconscionable to the extent that it would bar Harris from being awarded costs if she prevailed on her appeal." *Ante,* ---*N.J.* ---- (2006) (slip op. at 18).

***18** Because *Rudbart* plainly instructs that unconscionability is a concept that draws breath only from specific facts, the better view is the one adopted by Judge Lifland of the United States District Court for the District of New Jersey, who denied Harris's motion for summary judgment and granted Delta's cross-motion to compel arbitration, explaining that Harris's unconscionability claims require "a fact-sensitive analysis and must therefore be determined on a case-by-case basis." *Delta Funding Corp. v. Harris,* 396 *F.Supp.*2d 512, 516 (D.N.J.2004). Against that backdrop, Judge Lifland narrowed the issue to "[w]hether the Arbitration Agreement is an unenforceable contract of adhesion thus depends on whether it contains terms that are oppressive or unconscionable." *Id.* at 517.

In this certified question, I would not reach the merits of Harris's unconscionability claims. Therefore, in recognition of the limitation of *Rule* 2:12A-1, I would dismiss the certification of the question presented by the United States Court of Appeals for the Third Circuit as improvidently granted.

I respectfully dissent.

For the judgment-Chief Justice PORITZ and Justices LONG, LaVECCHIA and WALLACE-4.
For concurrence in part/dissent in part-Justice ZAZZALI-1.
For dissent-Justice RIVERA-SOTO-1.
Not Participating-Justice ALBIN.

> FN1. Harris and the amici who support her in this matter contend that there was substantial procedural unconscionability in this contract's formation. They

assert that Harris was presented with the arbitration agreement as part of many pages of mortgage documents that were brought to her home for signature at ten o'clock one evening. We do not attempt to resolve this or other factual disputes between the parties.

FN2. The arbitration agreement covers any claims involving "the validity, enforceability or *scope* of this [arbitration] Agreement." (Emphasis added).

FN3. Delta argues that if Harris brought her claim in the JAMS arbitration forum, the JAMS Policy on Consumer Arbitrations would shield her from incurring any more than $125 in arbitration costs. The application and interpretation of the JAMS policy is for the arbitrator to decide.

FN4. That said, the Appellate Division has enforced the customary provisions in mortgage notes that allow a lender, upon default, to recover from a borrower the costs of collection, including attorney's fees. *Hatch v. T & L Assocs.*, 319 *N.J.Super.* 644, 645, 647, 726 *A.*2d 308 (App.Div.1999). That situation is distinguishable from a contract in which a consumer asserting affirmative statutory claims may be required to bear the entire costs of arbitration.

FN5. According to Delta, we need not scrutinize the cost provisions of the arbitration agreement because it has offered to pay all of Harris's arbitration costs, thereby mooting any potential cost issues. We find that argument unpersuasive. As the Sixth Circuit has explained,

[i]n considering the ability of plaintiffs to pay arbitration costs under an arbitration agreement, reviewing courts should not consider after-the-fact

offers by employers to pay the plaintiff's share of the arbitration costs where the agreement itself provides that the plaintiff is liable, at least potentially, for arbitration fees and costs. The reason for this rule should be obvious. Our concern is that cost-splitting provisions will deter potential litigants from bringing their statutory claims in the arbitral forum. When the cost-splitting provision is in the arbitration agreement, potential litigants who read the arbitration agreement will discover that they will be liable, potentially, for fees if they bring their claim in the arbitral forum and thus may be deterred from doing so. Because the employer drafted the arbitration agreement, the employer is saddled with the consequences of the provision *as drafted.* If the provision, as drafted, would deter potential litigants, then it is unenforceable, regardless of whether, in a particular case, the employer agrees to pay a particular litigant's share of the fees and costs to avoid such a holding.
[*Morrison, supra,* 317 *F.*3d at 676-77.]

FN6. Under a different interpretation of this language, an arbitrator who refuses to consider granting a discretionary award of fees and costs to a party prevailing under RESPA would be acting "inconsistent with applicable law."

FN7. Delta counters that because the arbitration agreement requires the arbitrator to "apply applicable substantive law," the appeals cost provision does not bar an arbitrator from awarding Harris costs if she prevails on appeal.

FN8. The same conclusion was reached in *Cunningham v. Citigroup,* No. 05-3476, 2005 *U.S. Dist. LEXIS* 33805 (D.N.J. Dec. 16, 2005) (slip op. at

*16). In a well-reasoned analysis, the court in *Cunningham* noted that because "the right to pursue a foreclosure action can only be done through the court system, [an arbitration agreement exempting foreclosure proceedings from arbitration] is more a practical recognition of the limitations of the arbital [sic] forum rather than an unconscionable provision [under New Jersey law]." *Ibid.*

FN9. The arbitration clause states that "at the timely request of either party, [the arbitrator] shall provide a brief written explanation of the basis for the award."

N.J.,2006.
Delta Funding Corp. v. Harris
--- A.2d ----, 2006 WL 2277984 (N.J.)

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SUPREME COURT OF NEW JERSEY
M-255/256
September Term 2006
58,430

JALIYAH MUHAMMAD,

Plaintiff,

v. ORDER

COUNTY BANK OF REHOBOTH BEACH, DELAWARE; EASY CASH; TELECASH; and MAIN STREET CORPORATION,

Defendants-Movants.

ENTERED OCT 5 2006

This matter having been duly presented to the Court, it is ORDERED that the motion for reconsideration of the Court's Opinion (M-255) is denied; and it is further

ORDERED that the motion for an extension of time to file a motion for reconsideration (M-256) is granted.

WITNESS, the Honorable Deborah T. Poritz, Chief Justice, at Trenton, this 3rd day of October, 2006.

/s/
CLERK OF THE SUPREME COURT

WEIR & PARTNERS LLP
A Pennsylvania Limited Liability Partnership
Susan Verbonitz, Esquire
Marc J. Zucker, Esquire
20 Kings Highway West
Haddonfield, New Jersey 08033
(856) 740-1490
Attorneys for County Bank of Rehoboth Beach, Delaware

SWEENEY & SHEEHAN, P.C.
J. Michael Kunsch, Esquire
Sentry Office Plaza, Suite 500
216 Haddon Avenue
Westmont, NJ 08108
(856) 869-5600

MANATT PHELPH & PHILLIPS LLP
Claudia T. Callaway, Esquire
Pro hac vice
One Metro Center
700 12th Street N.W., Suite 1100
Washington, D.C. 20005
(202) 585-6504
Attorneys for Main Street Service Corp.

JALIYAH MUHAMMAD, on her own behalf and all others similarly situated, Plaintiff/Appellant,	:	SUPREME COURT OF NEW JERSEY
	:	Docket No. 58,430
v.	:	
COUNTY BANK OF REHOBOTH BEACH, DELAWARE, EASY CASH TELECASH AND MAIN STREET SERVICE CORPORATION, JOHN DOE AND JOHN ROE, Defendants/ Respondents	:	NOTICE OF MOTION FOR RECONSIDERATION OF COURT DECISION OF AUGUST 9, 2006

To: All counsel listed below:

PLEASE TAKE NOTICE that as soon as counsel may be heard, the undersigned attorneys for Defendants/Respondents, County Bank of Rehoboth Beach, Delaware and Main Street Service Corporation, shall move before the Supreme Court of New Jersey, Hughes Justice Complex, 25 West Market Street, Trenton, New Jersey 08625, for an order granting their Motion for Reconsideration of the Court's decision dated August 9, 2006. A copy of the Court's August 9, 2006 decision is attached to this Notice of Motion. In support of this Motion, Defendants/Respondents will rely upon the attached Memorandum of Law, containing the basis and ground of said Motion.

WEIR & PARTNERS LLP
A Pennsylvania Limited Liability Partnership

By:___/s/_____
Marc J. Zucker, Esquire
Susan Verbonitz, Esquire
20 Kings Highway West
Haddonfield, NJ 08033-2116
(856) 740-1490

Attorneys for County Bank of Rehoboth Beach Delaware

SWEENEY & SHEEHAN, P.C.

By:___/s/_____
J. Michael Kunsch, Esquire
Sentry Office Plaza, Suite 500
216 Haddon Avenue
Westmont, NJ 08108
(856) 869-5600

MANATT PHELPH & PHILLIPS LLP
Claudia T. Callaway, Esquire
One Metro Center
700 12th Street N.W., Suite 1100
Washington, D.C. 20005
(202) 585-6504

Attorneys for Main Street Corp.

To: Donna Siegel Moffa, Esquire
TRUJILLO, RODRIGUEZ & RICHARDS, LLC
8 Kings Highway West
Haddonfield, NJ 08033

Michael J. Quirk, Esquire Mark Cuker, Esquire
WILLIAMS CUKER BEREZOFSKY
One Penn Center at Suburban Station
1617 JFK Boulevard, Suite 800
Philadelphia, PA 19103-1819

William J. Pinilis, Esquire Pinilis Halpern LLP
237 South Street, Lower Level
Morristown, NJ 07960

Deborah M. Zuckerman, Esquire AARP Foundation
601 E Street, NW
Washington, DC 20049

Andrew B. Joseph, Esquire Drinker
Biddle & Reath LLP
500 Campus Drive
Florham Park, NJ 07932

Jeffrey J. Brookner, Esquire Wilentz,
Goldman & Spitzer
90 Woodbridge Center Drive
Suite 900, Box 10
Woodbridge, NJ 07095

Peter C. Harvey
Attorney General of New Jersey
R.J. Hughes Justice Complex
25 Market Street
Trenton, NJ 08625

JALIYAH MUHAMMAD, on her own behalf and all others similarly situated, Plaintiff/Appellant,	:	SUPREME COURT OF NEW JERSEY
	:	Docket No. 58,430
v.	:	
COUNTY BANK OF REHOBOTH BEACH, DELAWARE, EASY CASH TELECASH AND MAIN STREET SERVICE CORPORATION, JOHN DOE AND JOHN ROE, Defendants/ Respondents	:	PROOF OF SERVICE

I hereby certify that two true and correct copies of Defendants/Respondents' Motion for Reconsideration and this Certification of Service are being duly served upon each of the counsel for the Plaintiff/Appellant and amici applicants, by first class mail, on August 21, 2006, addressed as follows:

Donna Siegel Moffa, Esquire
TRUJILLO, RODRIGUEZ & RICHARDS, LLC
8 Kings Highway West
Haddonfield, NJ 08033

Michael J. Quirk, Esquire
Mark Cuker, Esquire
WILLIAMS CUKER BEREZOFSKY
One Penn Center at Suburban Station
1617 JFK Boulevard, Suite 800
Philadelphia, PA 19103-1819

William J. Pinilis, Esquire
Pinilis Halpern LLP
237 South Street, Lower Level
Morristown, NJ 07960

Deborah M. Zuckerman, Esquire
AARP Foundation
601 E Street, NW
Washington, DC 20049

Andrew B. Joseph, Esquire
Drinker Biddle & Reath LLP
500 Campus Drive
Florham Park, NJ 07932

Jeffrey J. Brookner, Esquire
Wilentz, Goldman & Spitzer
90 Woodbridge Center Drive
Suite 900, Box 10
Woodbridge, NJ 07095

Peter C. Harvey
Attorney General of New Jersey
R.J. Hughes Justice Complex
25 Market Street
Trenton, NJ 08625

I hereby certify that the foregoing statements made by me are true. I am aware that if any of the foregoing statements made by me are willingly false, I am subject to punishment.

/s/
Marc J. Zucker, Esquire

Dated: August 21, 2006

JALIYAH MUHAMMAD, on her own behalf and all others similarly situated, Plaintiff/Appellant,	: SUPREME COURT OF NEW JERSEY
	: Docket No.: 58,430
v.	:
COUNTY BANK OF REHOBOTH BEACH, DELAWARE, EASY CASH TELECASH AND MAIN STREET SERVICE CORPORATION, JOHN DOE AND JOHN ROE, Defendants/ Respondents	: ON INTERLOCUTORY REVIEW OF JULY 14, 2005 DECISION OF APPELLATE DIVISION STAYING ACTION AND COMPELLING ARBITRATION

SAT BELOW:
HON. HOWARD H. KESTIN, PJAD
HON. STEVEN L. LEFELT, JAD
HON. JOSEPH A. FALCONE, JAD
SUPERIOR CT OF NJ, APP. DIV.
Docet No. A-0558-04T3

MEMORANDUM OF LAW IN SUPPORT OF DEFENDANTS'/RESPONDENTS' MOTION FOR RECONSIDERATION

On the brief:

WEIR & PARTNERS LLP
A Pennsylvania Limited Liability Partnership
Marc J. Zucker, Esquire
Susan Verbonitz, Esquire
20 Kings Highway West
Haddonfield, New Jersey 08033
(856) 740-1490
Attorneys for County Bank of Rehoboth Beach, Delaware

SWEENEY & SHEEHAN, P.C.
J. Michael Kunsch, Esquire
Sentry Office Plaza, Suite 500
216 Haddon Avenue
Westmont, NJ 08108
(856) 869-5600
Attorneys for Main Street Service Corp.

Of counsel for Main Street Service Corp.:
MANATT PHELPH & PHILLIPS LLP
Claudia T. Callaway, Esquire
Pro hac vice
One Metro Center
700 12th Street N.W., Suite 1100
Washington, D.C. 20005
(202) 585-6504

Date: August 21, 2006

PRELIMINARY STATEMENT

As this Court noted, its August 9, 2006 holding that NewJersey law on unconscionability prohibits class arbitration waivers in "low value" consumer arbitration agreements represented its first articulation of this legal principle. The decision likewise is novel in elevating the procedural device of class arbitration, never previously addressed by the Court, into a substantive right under certain circumstances.

The effects of the Court's ruling are both global and casespecific. On a global level, the Court's ruling disregards the preemptive effect of the Federal Arbitration Act, 9 U.S.C. §§116 ("the FAA"), because it interprets New Jersey law in a way that discriminates against arbitration agreements in certain consumer contracts. The Court's ruling invites arbitrary interpretation among the lower courts of this state, as well as forum shopping between state and federal courts in New Jersey, because it gives no guidance regarding its newly-created distinction between "high" and "low" value consumer claims. The Court is unable to cure this problem through line drawing because any attempt to do so would itself be arbitrary. By severing the class arbitration waiver from the arbitration agreement, the Court has redrafted the parties' agreement in a way that conflicts with the letter and spirit of the FAA, again subjecting New Jersey law to federal preemption, and more immediately, creating uncertainty for New Jersey's lower courts, consumers and businesses.

In addition the Court's ruling presents problems specific to the instant case:

- The ruling presents federal and equitable due process and dormant commerce clause concerns because it applies a new interpretation of New Jersey law retroactively to the arbitration agreements at issue here,

unduly burdens commerce and effects a wholesale modification to the nature of the parties' bargain.

- The ruling is based on findings of "facts" not contained in the record on appeal.
- The Court should have considered defendants' arguments regarding the Delaware choice of law clause contained in the contracts at issue. Defendants invite the Court to give full consideration to its choice of law arguments, and/or remand for the trial court to do so.

For all of these reasons, defendants respectfully request that the Court reconsider its August 9, 2006 ruling in this matter.

ARGUMENT

I. FEDERAL LAW PREEMPTS THIS COURT'S HOLDING THAT CLASS WAIVERS ARE UNCONSCIONABLE.

State law is preempted whenever it "stands as an obstacle to the accomplishment and execution of the full purposes and objectives of Congress." *Fid. Fed. Sav. & Loan Assn v. de la* ***Cuesta,*** 458 U.S. 141, 153 (1982) (internal quotation marks omitted). In declaring class arbitration waivers unenforceable in "low" value **cases,** this Court has placed its own policy preference for class actions squarely above Congress's policy of ensuring the enforcement of arbitration **agreements** as written. ***See, e.g.,*** *Mastruobuono v. Shearson Lehman* Hutton, *Inc.*, 514 U.S. 52, 53-54 (1995) ; *Volt Info. Scis., Inc. v. Bd. of Trs. of Leland Stanford Jr. Univ.,* 489 U.S. 468, 475 (1989). When state and

Congressional policies clash, Congress prevails. *Perry v. Thomas,* 482 U.S. 482, 491 (1987).[1]

The FAA preempts state laws which arbitrarily hinder arbitration, including state law which prohibits class action waivers. *See Schultz v. AT&T Wireless Services, Inc.,* 376 F. Supp. 2d 685 (N.D.W.V. 2005). In *Shultz,* a West Virginia district court concluded that, if West Virginia law were read to preclude class action waivers, it would run afoul of the FAA and be preempted. The court cited a number of federal cases holding that the FAA preempts "state rules of contract formation which single out arbitration clauses and unreasonably burden the ability to form arbitration agreements." *Id.* at 689, 690 (quoting *Saturn Distrib. Corp. v. Williams,* 905 F.2d 719, 723 (4th Cir. 1990)). *Shultz* rejected an argument that West Virginia law enshrined a right to class actions that could not be vitiated by an arbitration clause, and concluded that "the plaintiffs argument that the arbitration clause is unconscionable due to its foreclosure of class action relief also lacks merit." *Id.* at 691.

The conflict contemplated in *Schultz* is the precise problem presented in Muhammad. Aside from conflicts with

---

[1] The United States Supreme Court has long recognized that, "[i]f the federal court allows arbitration where the state court would disallow it, the outcome of litigation might depend on the courthouse where suit is brought." *Bernhardt v. Polygraphic* Co., 350 U.S. 198, 203 (1956). The converse, of course, is equally true: . Parties to a contract evidencing interstate commerce should not be permitted to avoid arbitration by filing their action in a state court when,, had the action been brought in federal court, they would have been compelled to arbitrate. *See Burke Co. Public Sch. Board of Education v. Shaver Partnership,* 303 N.C. 408 (1981). To prevent such conflicts, Congress specifically imbued the FAA with preemptive force-where state and federal law would result in disparate rulings, the state burdening arbitration while federal law promotes it, the federal law must govern.

other appellate courts, the decision at bench conflicts with *Johnson v. West Suburban* Bank, 225 F.3d 366, 374 (3d Cir. 2000), thereby creating confused and conflicting law for New Jersey litigants.

Until now, the jurisprudence of this state did not conflict with the FAA. Having now articulated a new interpretation of the law, the Court's ruling will be preempted because, as demonstrated in the succeeding sections, it directly conflicts with the FAA, in letter and in spirit.

II. A RULE AGAINST CLASS ARBITRATION WAIVERS FOR "LOW VALUE CONSUMER CLAIMS" NECESSARILY DISCRIMINATES AGAINST ARBITRATION AND FRUSTRATES THE PURPOSES OF THE FAA.

The enforceability of an arbitration agreement does not and cannot depend on the value of the claims sought to. be arbitrated. To subject arbitration agreements to such an *ad hoc* standard for enforceability, which is not generally applicable to other types of contracts, violates the FAA. *See Martindale v. Sandvik, Inc.*, 173 N.J. 76, 86 (N.J. 2002) *(quoting Perry v. Thomas,* 482 U.S. at 492 n.9 (1987) ("[S]tate law, whether of legislative or judicial origin, is applicable if that law arose to govern issues concerning the validity, revocability, and enforceability of contracts generally." However, states may not "decide that a contract is fair enough to enforce all its basic terms but not fair enough to enforce its arbitration clause" because "that kind of policy would place arbitration clauses on an unequal 'footing,' directly contrary to the Act's language and Congress' intent.") See also, *Schultz v. AT&T Wireless Services, Inc.*, 37 F. Supp. 2d 685, 690-91 (2005) ; *Park v. Merrill Lynch,* 159 N.C. App. 120, 122, 582 S.E.2d 375, 378 (2003).

Though true that the FAA permits states to regulatearbitration agreements, including enforcing or rejecting such agreements on "grounds as exist at law or in equity for the revocation of any contract," 9 U.S.C. § 2, the unconscionability rule applied in this case is not a ground that exists for *any* contract, but rather *only* for the narrow class of terms or agreements relating to the procedures available to claimants in arbitration, and *only* to certain entities whose business may generate small dollar consumer claims. In short, New Jersey's general rule on unconscionability does not prohibit arbitration agreements, or even arbitration agreements containing class waivers. There was no federal conflict until this Court created the new subcategory of cases that this Court has ambiguously named "low value consumer claims."

Indeed, this arbitrary line between "low value" and "high value" loans would also prove unworkable in practice, because it necessarily would invite courts to draw *post hoc,* arbitrary lines between claims that are substantial "enough" to merit individual arbitration and claims that are thought to be too small to justify it, and without knowing the size of claims to be asserted by other members of the putative class. *Compare, Muhammad* with *Delta Funding Corp. v. Harris,* 2006 WL 2277984 (N.J. 2006); *see Allied-Bruce Terminix Cos. v. Dobson,* 513 U.S. 265, 282 (1995) (O'Connor, J., concurring) (emphasizing that courts should avoid interpreting FAA in a way that would "foster pre-arbitration litigation that would frustrate the very purpose of the statute"). If such a bright line should be drawn, Congress is in the best position to draw it.

The Court's opinion articulates a preference for class actions over the policy preference of Congress in enacting the FAA: to ensure enforcement of arbitration provisions as written. *See, e.g., Mastrobuono v. Shearson Lehman* Hutton, *Inc.,* 514 U.S. 52, 53-54 (1995); *Volt Info., supra,* 489 U.S.

at 479; *Dean Witter Reynolds, Inc. v. Byrd,* 470 U.S. 213, 219-221 (1985). As noted above, when state and Congressional policies clash on, application of the FAA, the latter must prevail. *Perry v. Thomas,* supra, 482 U.S. at 491.

III. SEVERING THE CLASS ARBITRATION WAIVER RESULTS IN THE EFFECTIVE DENIAL OF DEFENDANTS' MOTION TO COMPEL ARBITRATION AND VIOLATES THE DUE PROCESS CLAUSE OF THE UNITED STATES CONSTITUTION.

Respectfully, this Court's decision to sever. the class waiver effectively denies defendants' motion to compel arbitration while purporting to compel it. Moreover, severing the arbitration agreement is hostile to the FAA, contrary to the agreement of the parties, and is a violation of defendants' due process rights under the 14th Amendment of the U.S. Constitution.

Section 2 of the FAA declares pre-dispute arbitrationagreements "valid, irrevocable, and enforceable" because "arbitration saves time, saves trouble, saves money." Joint Hearings on S. 1005 and H.R. 646 Before the Subcomms. of the Comms. on the Judiciary, 68th Cong., 1St Sess. 7 (1924) (statement of Charles Bernheimer, N.Y. Chamber of Commerce). As Congress later explained, arbitration usually is "cheaper and faster than litigation," has "simpler procedural and evidentiary rules," "minimizes hostility," and is "more flexible in regard to scheduling." H.R. Rep. No. 97-542 a 13 (1982). A limitation in an arbitration agreement precluding class actions or arbitrations is essential to preserve the "simplicity, informality, and expedition of arbitration." *Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc.,* 473 U.S. 614, 628 (1985).

The Court's decision to eliminate class arbitration waivers effectively denies defendants the benefit of their bargain, and threatens to subject them to a massive procedural morass and chilling threat of limitless damages. Whether conducted by a court or by an arbitrator, all of the procedures necessary to the fair administration of a class action will make arbitration much more expensive and time consuming. In fact, many commentators believe that "class arbitration may actually prove more burdensome than class litigation" because the simplified procedures in arbitration were never designed with class actions in mind. Jack Wilson, "No-Class-Action Arbitration Clauses," State-Law Unconscionability and the Federal Arbitration Act: A Case For Federal Judicial Restraint and Congressional Action, 23 Quinnipiac L. Rev. 737, 774 (2004). Subjecting the parties to class arbitration has the same (or worse) effect as denying defendants' motion to compel arbitration and ordering the case to proceed in court as a class action, and the Court's ruling is not saved by blue penciling the parties' agreement.

Indeed, the severance is more than the mere removal of a few words which the Court believed to be unconscionable. It effects a wholesale re-writing of the parties' agreement, qualitatively (and, as discussed in greater detail below, retroactively) changing a contract among three parties - a borrower (Muhammad), lender (County Bank) and servicer (Main Street) - into one with potentially thousands of other parties.

Moreover, the Court's holding is directly in conflict with the U.S. Supreme Court's holding in *Green Tree Financial v. Bazzle,* 539 U.S. 444, 451-52 (2003). In *Bazzle,* the Court held that the question of whether the parties' dispute was subject to class arbitration did not fall into the narrow exception of arbitration-related matters intended to be decided by a court instead of an arbitrator. Rather, such an issue was itself arbitrable, and therefore was for the

arbitrator, not the courts, to decide. *Id.* Where, as here, the arbitration agreement clearly reflected an intent against class arbitration, the result should be no different. An arbitrator, not a court, should decide whether the parties, expressed intent must be disregarded.

IV. THE COURT'S RULING ARTICULATES A NEW INTERPRETATION OF NEW JERSEY LAW AND SHOULD NOT BE APPLIED RETROACTIVELY.

In its Opinion, this Court expressly noted that the issue of class arbitration "specifically has never before been examined by this Court." Opinion at 17-18. The Court also acknowledged that the legislature did not provide guidance on the issue of class arbitration, noting that " [c] lass arbitration is in its infancy and may provide a fertile ground for establishing flexible class-action procedures" and advising that "the United States Congress and/or [the] State Legislature may amend class-action procedures should they perceive deficiencies in the current process." Opinion, at 28. Indeed, the ruling is doubly novel in elevating the class action, for the first time, from a procedural device to a substantive right. Because the Court has articulated a new legal principle, it would violate defendants, due process rights to apply that decision retroactively to these parties.

New Jersey law prior to Muhammad held that a waiver of certain rights in an arbitration clause would be enforced so long as they were sufficiently notorious and specific. *Gras v. Associates First Capital Co.,* 346 N.J. Super. 42, 49-57 (App. Div. 2001), *cert. denied,* 171 N.J. 445 (2002). In *Muhammad,* the Court distinguished between "low value" and "high value" plaintiffs' claims in determining that a class arbitration waiver is unconscionable and unenforceable when it involves an undefined small amount of money, while a separate ruling on the same day in

Delta Funding, supra, held that such waivers *were* enforceable and not unconscionable when they involved a larger monetary claim. The Court has retroactively applied its holding to invalidate literally thousands of similar agreements containing express waivers of a consumer's ability to bring a class action in arbitration.

While the Court may determine that its ruling must stand, it should not be applied retroactively to the parties here because to do so would. cause manifest injustice. Retroactivity is generally disfavored in the law. *Bowen v. Georgetown Univ. Hospital,* 488 U.S. 204, 208 (1988), see H. Broom, Legal Maxims 24 (8th ed. 1911) ("Retrospective laws are, as a rule, questionable policy, and contrary to the general principle that legislation by which the conduct of mankind is to be regulated ought to deal with future acts, and ought not to change the character of past transactions carried on upon the faith of the then existing law").. Both federal and New Jersey law establish that there are explicit and implied limitations on the legislature's power to impose laws retroactively. Article I, Section 10 of the U.S. Constitution provides that "[n]o State shall…pass any...law impairing the obligation of contracts." Just as legislatures are barred, so are the courts.

All statutes with retroactive elements are subject to scrutiny under the due process clause of the Fourteenth Amendment of the U.S. Constitution and the parallel provision of the New Jersey Constitution. U. S. Const. amend. XIV, § 1; N.J.Const., art. 1, ¶ 1. In fact, a court may not automatically apply a change in the law retroactively where the application of that law attaches new legal consequences to completed, past conduct that was legal at the time. *Usery v. Turner Elkhorn Mining Co.,* 428 U.S. 1, 15-16 (1976). In adopting the *Usery* standard, this Court determined that "[a] consistent line of decisions by the United States Supreme Court interpreting the Due Process

Clause of the Fourteenth Amendment holds that retroactive legislation does not deprive parties of due process if the legislation "is supported by a legitimate legislative purpose furthered by rational means." Nobrega v. *Edison Glen Assoc.,* 167 N.J. 520, 543 (N.J. 2001), *citing Pension Ben. Guar. Corp. v. R.A. Gray & Co.,* 467 U.S. 717, 729 (1984).

As this Court held in *Montells v. Haynes,133* N.J. 282, 295, 627 A.2d 654,660 - 661 (1993):

> Prospective application is appropriate when a decision establishes a new principle of law by overruling past precedent or by deciding an issue of first impression. *Coons v. American Honda Motor Co.,* 96 N.J. 419, 427, 476 A.2d 763 (1984), cert. denied, 469 U.S. 1123, 105 S.Ct. 808, 83 L.Ed.2d 800 (1985) (Coons II). Together with those considerations, we must also weigh whether retroactivity furthers the underlying purpose of the rule and whether retroactive applications could produce substantial inequitable results. *Coons II, supra,* 96 N.J. at 427, 476 A.2d 763. As *Coons II* states, our case law roughly parallels that of the United States Supreme Court on the issue of prospectivity. 96 N.J. at 428, 476 A.2d 763. In reversing a decision that followed the general rule of retrospective effect, *Coons II* applied "principles drawn from our own state court decisions as well as from United States Supreme Court cases." Id. at 425, 476 A.2d 763. Coons II recognized that *Chevron Oil Co. v. Huson,* 404 U.S. 97, 92 S.Ct. 349, 30 L.Ed.2d 296 (1971), best typified federal prospectivity analysis. Just last month, however, the United States Supreme Court cast doubt on the continuing vitality of Chevron's prospectivity analysis in cases of federal law. *Harper V. Virginia Department* of Taxation, 509 U.S. 86, 113 S.Ct. 2510, 125 L.Ed.2d 74 (1993).

> Whatever path that Court may follow, we believe that in an appropriate case a purely prospective application may provide the fairest and most equitable disposition.

133 N.J. at 295, 627 A.2d at 660 - 661.

In this case, there is no legitimate purpose for retroactive application of the new rule articulated by the Court. Indeed, the Court's holding is directly contrary to the legitimate state and federal policy favoring the resolution of disputes through arbitration. In addition, the Court's distinction between the claims in *Delta Funding* and those in *Muhammad* does not meet the "rational means" prong of the *Usery* test because the Court has chosen to draw arbitrary lines based on the undefined value of claims - including unknown claims of putative class members - rather than articulating a rule that can be uniformly applied.

In addition to the constitutional due process inquiry, this Court has determined that a statute (or case law interpreting a statute) may not be applied retroactively if to do so would cause a manifest injustice. *Nobrega, supra,* 167 N.J. at 545. "The concern that is implicated by the standard of `manifest injustice' in assessing the retroactive application of a statute need not reach constitutional levels. Hence, while our inquiry into whether there has been a `manifest injustice' is informed by our consideration of issues of constitutional due process, it is not necessarily determined by those issues." *In re D. C.,* 146 N. J. at 58. The essence of the manifest injustice inquiry is whether the affected party relied, to his or her prejudice, on the law that is now to be changed as a result of the retroactive application of the law, and whether the consequences of this reliance "are so deleterious and irrevocable that it would be unfair to apply the statute retroactively." *Gibbons v. Gibbons,* 86 N.J. at 523-25.

As set forth above, the Court's ruling in *Muhammad* effectively may be deemed to invalidate thousands of existing contracts in which the parties expressly waived certain rights to court proceedings and class actions, and impacts every lender and merchant that offers credit cards to New Jersey residents, as well as all sellers of retail consumer goods that rely on class action waivers in arbitration agreements. Such a sweeping application of a fact-specific analysis is arbitrary and irrational and cannot be the basis for retroactive application of this ruling. *Usery, supra,* 428 U.S. at 15. Not only does the ruling in *Muhammad* impose additional obligations on defendants that were not negotiated by the parties, but these terms directly contradict the express agreement of the parties. A retrospective application of the ruling in *Muhammad* will result in lengthy and expensive class action arbitration against defendants that was not anticipated by the parties at the time of entering into the contract, and it will have the chilling. effect of discouraging other businesses from doing lending in this so-called "low value" arena, an area in which customers arguably need additional options, not fewer.

These burdens implicate not only the due process clause but also the dormant commerce clause, as applied by the U.S. Supreme Court. *See, BMW of North America, Inc. v. Gore,* 517 U.S. 559, 572 n. 17 (1996); *Ileto v. Glock Inc.,* 349 F.3d 1191, 1217 (9th Cir. 2003)(noting in dicta that a dormant commerce clause claim may be premised on court action in a civil lawsuit).

V. THE NON-RECORD FINDINGS AND ASSUMPTIONS RELIED UPON BY THIS COURT SHOULD BE RECONSIDERED OR TESTED ON REMAND.

In support of its holding that the class arbitration waiver contained in the parties' arbitration agreements is unconscionable under New Jersey contract law, the Court made a series of factual findings and assumptions which either had no foundation in, the trial court record or were contrary to the facts of record. Among those findings were the following:

- The Court found that Muhammad's "small" damage claim "render[s] individual enforcement of her rights, and the rights of her fellow consumers, difficult if not impossible." Id. at 22. It found further that "the availability of attorney's is illusory" because "it is unlikely that counsel would be willing to undertake the representation." *Id.* at 24. Respectfully, these findings are not supported by the trial court record, and to the contrary are contradicted by the trial court's conclusion that Muhammad was able to vindicate her rights in an individual arbitration. (PA761-800).[2]

---

[2] Muhammad alleges violation of the New Jersey Consumer Finance Act against the marketers (Count I) and County Bank (Count II) ; usury against the marketers (Count III) ; violation of New Jersey's RICO statute against the marketers (Count IV); and conspiracy to violate RICO against County Bank (Count V). She seeks a return of all monies paid on the usury claims, and a subsequent trebling of that amount against each defendant for the Consumer Finance Act and RICO claims, *plus* pre-judgment interest and attorney fees.

As noted above, no information whatsoever is known about the size of claims of other putative class members.

- The Court found that the instant case involves complicated financial arrangements (Opinion at 26), even though the loan transaction at issue was a small consumer loan, evidenced by a one-sided, single page note, transacted over a fax machine.

- The Court found that the arbitration agreements contain limits on discovery (Opinion, p. 21), even though the arbitration agreements do not mention discovery.

- The Court found that Muhammad and other members of the putative class are under a high degree of economic compulsion, "compelling their acquiescence to loans bearing exorbitant interest rates" (id., fn. 4), even though there is no evidence on the record that either Muhammad or any other consumer who obtained a loan from County Bank was under such compulsion.

Focusing for a moment solely on the Court's "complexity" and "low value" findings, both *Muhammad* and *Delta Funding Corp. v. Harris,* No. A-44-05 (N.J. Aug. 9, 2006), involve transactions by individual consumers with multiple, heavily regulated, out-of-state financial services entities. As a predicate to severing the prohibition on class arbitration in the former but not in the latter, the Court found that the transaction in *Muhammad* was "complicated" and that its complexity was a factor that precluded enforcement of the prohibition on class arbitration. See Muhammad, Slip Op. at 25 ("One may be hard pressed to find an attorney

willing to work on a consumer-fraud complaint involving complex arrangements between financial institutions of other jurisdictions when the recovery is so small."). Ignoring the provisions in the contract and pertinent statutes for damages-multipliers, recovery of costs and attorneys fees, as well as substantial precedent to the contrary, the Court instead summarily concluded that no attorney would be willing to represent a consumer in such a ".complex" case absent-a potential windfall recovery in the form of contingency fees. *Muhammad* Slip Op. at 18 (noting that "attorney's actual fees" insufficient incentive to bring action).

In a recent case squarely on point, the First Circuit explicitly held that a deferred-deposit short-term loan identical in all material respects to that at issue in Muhammad did not present the sort of factual complexity that may necessitate the severance of an arbitration provision barring use of class mechanisms. See *Kristian v. Comcast Corp.*, 446 F.3d 25 (1st Cir. 2006). Distinguishing the decisions of four other circuits that enforced consumer arbitration provisions barring class mechanisms (including the Third Circuit), the Court found that an antitrust action was inherently more complex than the transactions at issue in those cases and severed these provisions from the arbitration agreement. The Court distinguished *Snowden v. CheckPoint Check Cashing,* 290 F.3d 631 (4th Cir. 2002), in which the Fourth Circuit had upheld a provision barring class mechanisms in a dispute over a short-term loan transaction that was identical in all material respects to that at issue in *Muhammad.* The Court found that,

> In a case such as *Snowden,* there is a specific transaction at issue... This is not a particularly difficult ,analysis....

Kristian, 446 F.3d at 57-58 (citation omitted). As the First Circuit recognized, where as here, the terms governing the

parties' relationship (including the relationship between County Bank and Main Street Service Corp.) are clearly set forth in a comparatively short written agreement, the applicable law is straightforward and well settled.

The assumptions made by the Court regarding the size of plaintiff's claim and the complexity of her case have no support in the record and therefore should not have been relied upon. *See Cipala v. Lincoln Technical institute,* 179 N.J. 45, 52, 843 A.2d 1069 (2004). To the extent factual findings such as those articulated by the Court are necessary to determine the issue of unconscionability, then the matter should be remanded to the trial court for such additional findings.

VI. ON RECONSIDERATION, OR ON REMAND, A COURT MUST DETERMINE WHETHER DELAWARE LAW APPLIED TO THE UNCONSCIONABILITY ANALYSIS.

In the course of addressing the enforceability of the classarbitration waiver, the Court articulated and applied new principles of New Jersey law, (Opinion, pp. 31, 32), despite the fact that, to the extent state law applies at all, the parties' contract, including .the arbitration agreement, is governed by the state law of Delaware.

The three contracts signed by Muhammad contain a clear and prominent Delaware choice of law provision (Pal86-188). Muhammad accepted the choice of Delaware law in connection with this transaction and made no attempt at the trial court level or on appeal to challenge the Delaware choice-of-law clause in the agreements she signed. To the contrary, Muhammad conceded that, as a Delaware state-chartered bank, County Bank is not subject to New Jersey law. (Pa10, 329), and acknowledged that among the rights

Muhammad waived was "the right to have New Jersey law apply." (Pa330) .

The Appellate Division stated in footnote 3 of its opinion that the choice-of-law issue was not briefed or addressed in the trial court, but rather was asserted by defendants in a footnote in their appellate brief. *Muhammad v. County Bank of* Rehoboth *Beach,* 379 N.J.Super. 222, 234 n.3, 877 A.2d 340, 347 n.3 (App.Div. 2005). In fact, despite Muhammad's concession that as a Delaware state-chartered bank, County Bank is not subject to New Jersey law, and her failure to challenge the Delaware choice of law clause in the agreements she signed, defendants nevertheless *raised the issue repeatedly* before the trial court and on appeal. *(See* Pa36, 43, 611 n. 3, 627; *see also,* February 11, 2005 appellate division reply brief in response to amici at pp. 9-11, devoting an entire section to this argument).

While maintaining the mistaken view that the application of Delaware law had been raised solely in a footnote, the Appellate Division affirmed the trial court's order compelling arbitration and staying the proceedings. Given the favorable ruling, defendants had no reason to seek review of the Appellate Division's choice of law discussion, which itself was relegated to a footnote. 379 N.J.Super. at 234 n.3, 877 A.2d at 347 n.3. Indeed, since the Appellate Division's enforcement of the class action waiver suggested that there was no conflict between Delaware and New Jersey law, no conflict of laws analysis was warranted. *Fu v. Fu,* 160 N.J. 108, 733 A.2d 1133 (1999) (first prong of conflict analysis is whether there is an actual conflict).

On appeal to this Court, defendants once again devoted a section of their brief to the choice of law issue, offering this Court an alternate ground upon which to affirm the Appellate Division. (Db17-18) Nevertheless, in its August 9, 2006 opinion, this Court chose not to address the choice of

law issue, concluding in footnote 2 that defendants "did not seek review of the Appellate Division's determination of that issue," and thereby hinting that defendants should have filed a cross-appeal relating thereto and had waived the issue by not doing so. Respectfully, such a procedure was neither required nor appropriate under the circumstances, given defendants' unqualified victory below and the absence, until now, of a conflict between the law of New Jersey and Delaware on this issue.

Appeals are taken solely from orders or judgments, not judicial opinions. *Heffner v. Jacobson,* 100 N.J. 550, 553, 498 A.2d 766 (1985). *See Credit Bureau Collection Agency v. Lind,* 71 N.J. Super. 326, 328, 177 A.2d 36 (App. Div. 1961) ("An appeal lies not from a written or oral decision of the court, but only from a judgment or order.") A respondent is not required to file a cross-appeal in order to raise any argument supported by the record in defense of a judgment entered below. Only when the respondent seeks to obtain relief from any portion of the ***judgment*** entered below is a cross-appeal necessary. The respondent can argue any point on appeal to sustain the trial court's order. *New Jersey State Firemen's Mut. Benev. Ass'n. v. North Hudson Regional Fire & Rescue,* 340 N.J. Super. 577, 775 A.2d 43 (App. Div. 2001); *New Jersey Div. of Youth and Family Services v. B.G.S.,* 291 N.J. Super. 582, 677 A.2d 1170, 1172-1174 (App. Div. 1996).[3]

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[3] Moreover, an appellate court is capable of affirming the lower court's grant of relief to a respondent in the absence of a cross-appeal if that relief will sustain the trial court's judgment. *Chimes v. Oritani Motor Hotel, Inc.,* 195 N.J. Super. 435, 480 A.2d 218, 222 (App. Div. 1984). This allows the respondent to raise an alternate theory to sustain the trial court's judgment, without the necessity of filing a cross-appeal. Id. at 222 (holding that "a respondent can argue any point on the appeal to sustain the trial court's judgment," because "appeals are taken from judgments, not opinions.")

As a result of this Court's August 9 decision, there now exists a clear conflict between the law of New Jersey and Delaware on the enforceability of class arbitration waivers. Respectfully, the Court should direct the trial court to determine on remand whether Delaware law governs the unconscionability analysis of the arbitration agreement.

CONCLUSION

For all of the foregoing reasons, defendants-respondents respectfully request that this Court reconsider its ruling and affirm the decisions below. Should the Court decline reconsideration, defendants respectfully request that the case be remanded with additional instructions for the trial court to first determine whether the parties' choice of law provision should be enforced and second, for the trial court to make findings of fact to determine whether the assumptions underlying this Court's ruling are actually present in this case.

Respectfully submitted,

WEIR & PARTNERS LLP
A Pennsylvania Limited Liability Partnership

By: /s/
Marc J. Zucker, Esquire
Susan Verbonitz, Esquire
20 Kings Highway West
Haddonfield, New Jersey 08033
(856) 740-1490
Attorneys for County bank of Rehoboth Beach, Delaware

SWEENEY & SHEEHAN, P.C.

By: /s/
J. Michael Kunsch, Esquire
Sentry Office Plaza, Suite 500
216 Haddon Avenue
Westmont, NJ 08108
(856) 869-5600

MANATT PHELPH & PHILLIPS LLP
Claudia T. Callaway, Esquire (*Pro hac vice*)
One Metro Center
700 12th Street N.W., Suite 1100
Washington, D.C. 20005
(202) 585-6500

Attorneys for Main Street Service Corp.

SUPREME COURT OF NEW JERSEY

NO. 58,430

JALIYAH MUHAMMAD	:	ON APPEAL FROM THE
	:	SUPERIOR COURT OF
	:	NEW JERSEY,
Plaintiff-Appellant	:	APPELLATE DIVISION
	:	
v.	:	DOCKET NO. A-0558-04T3
	:	
COUNTY BANK OF	:	
REHOBOTH BEACH,	:	
DELAWARE; EASY CASH;	:	
TELECASH; and MAIN	:	
STREET CORPORATION	:	
	:	
Defendants-	:	
Respondents	:	
	:	

SAT BELOW:
HON. HOWARD H. KESTIN, PJAD
HON. STEVEN L. LEFELT, JAD
HON. JOSEPH A. FALCONE, JAD

BRIEF OF *AMICUS CURIAE* CHAMBER OF COMMERCE OF THE UNITED STATES OF AMERICA IN SUPPORT OF RESPONDENTS

OF COUNSEL

MAYER, BROWN, ROWE & MAW LLP
Evan M. Tager (*pro hac vice*)
David M. Gossett (*pro hac vice*)
1909 K Street, NW
Washington, DC 20006
(202) 263-3000

NATIONAL CHAMBER LITIGATION CENTER, INC.
Robin S. Conrad (*pro hac vice*)
Amar D. Sarwal (*pro hac vice*)
1615 H Street, NW
Washington, DC 20062
(202) 463-5337

Andrew B. Joseph
DRINKER BIDDLE & REATH LLP
A Pennsylvania Limited Liability Partnership
500 Campus Drive
Florham Park, NJ 07932
Telephone: (973) 360-1100

Attorneys for Chamber of Commerce of the
United States of America

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INTEREST OF THE AMICUS CURIAE

The Chamber of Commerce of the United States of America (the "Chamber") is the world's largest business federation, representing an underlying membership of more than 3 million businesses and organizations of all sizes. Many of the Chamber's members, constituent organizations, and affiliates have adopted as standard features of their business contracts provisions that mandate the arbitration of disputes arising from or related to those contracts. They use arbitration because it is a prompt, fair, inexpensive, and effective method of resolving disputes with consumers and other contracting parties.

In this case, appellant Jaliyah Muhammad joins a growing (and disturbing) bandwagon of parties who seek to avoid arbitration agreements by use of state-law unconscionability principles. If this Court were to nullify the arbitration agreement at issue here on unconscionability grounds, it would wreak havoc on countless arbitration provisions in contracts entered into by the Chamber's members. Such an outcome would be gravely troubling because the business community has substantially relied on arbitration provisions - indeed, businesses have structured millions of contractual relationships around them - in light of the U.S. Supreme Court's consistent endorsement of arbitration over the past several decades as a favored means of dispute resolution. Thus, the Chamber has a strong interest in explaining why this Court should hold thatthe arbitration agreement at issue here is enforceable.

PRELIMINARY STATEMENT

Although Muhammad and her *amici* raise a litanychallenges to the parties' arbitration agreements, in this brief we focus on a subset of those attacks that are especially important to the business community as a whole.

1. Because of its importance to businesses and consumers in New Jersey and throughout the nation, we initially focus on the question whether a court may rely upon a requirement that arbitration proceed on an individual basis to invalidate an arbitration provision. See Muhammad Br. 16-24 (arguing that class waiver renders arbitration agreements unconscionable). There are a number of reasons why a court may not do so. To begin with, we agree with respondents (collectively "County Bank") that because the prohibition on class actions is contained in a provision of Muhammad's contracts that is separate from the arbitration provision and would by its terms apply not only in arbitration but also in court, the question of the enforceability of that waiver of class actions is reserved for an arbitrator to decide. But even if this Court were to reach the issue, neither New Jersey nor Delaware unconscionability law supports the invalidation of class waivers. Indeed, a holding that the class waiver in this case is unconscionable would necessitate distorting New Jersey (and Delaware) unconscionability law. Consequently, such a holding would be expressly preempted by Section 2 of the Federal Arbitration Act ("FAA"), *9 U.S.C.* § 2, which specifies that arbitration provisions may be invalidated only on the basis of state-law principles that apply neutrally to all contractual provisions. Such a holding also would be impliedly preempted by the FAA because conditioning the enforceability of arbitration provisions on the availability of class arbitration would strongly discourage the inclusion of such provisions in contracts.

2. Muhammad also argues that the Court should give no weight to County Bank's offer to pay the full costs of arbitration and to submit to individual arbitration before the American Arbitration Association, which she had suggested in her trial-court briefing is a preferable forum to the National Arbitration Forum (the arbitration provider designated in her contracts). As we explain below, numerous

courts around the country have held that offers by a company to waive challenged features of an arbitration provision moot challenges to the enforceability of the arbitration provision based on the waived features. This practice is eminently sensible: it ensures that customers will resolve disputes in an arbitral forum (as they have agreed to do), thereby effectuating the federal policy favoring the enforcement of arbitration provisions.

2. Muhammad's reliance on policy challenges to "payday lending" as a basis for invalidating her arbitration agreement is an improper diversion because she is not entitled to attack the validity of the underlying contract in this proceeding. As the U.S. Supreme Court made clear nearly four decades ago, an arbitration agreement is separable from the remainder of a contract, and its enforceability must be determined independently from an analysis of any challenge to the contract as a whole.

3. Finally, in resolving the issues in this case, the Court should reject the hostility to standard form contracts that so evidently underlies Muhammad's arguments. Form contracts of the sort involved here are critically necessary to the modern economy. As a consequence, any rule that categorically impairs the enforceability of form contracts would have devastating implications for both businesses and consumers.

PROCEDURAL HISTORY AND STATEMENT OF FACTS

Plaintiff-appellant Jaliyah Muhammad entered into three short-term loan agreements (so-called "payday loans") with County Bank. As part of these contracts, Muhammad agreed to arbitrate her disputes with County Bank. Muhammad v. County Bank *of Rehoboth Beach, Del.*, 379 *N.J. Super.* 222, 229 (App. Div. 2005). Muhammad's

contracts also contained a separate provision under which she agreed not to pursue or participate in class actions. Id.

Notwithstanding her contractual agreements, Muhammad filed a putative class action lawsuit in Superior Court against respondents, alleging violations of the New Jersey Consumer Fraud Act, New Jersey's racketeering statute, and New Jersey's usury laws. See id. at 230-31. County Bank removed the case to federal court and moved to compel arbitration. The federal court remanded to state court without ruling on the arbitration motion. Thereafter, County Bank again moved to compel arbitration under Muhammad's agreements. The superior court granted County Bank's motion, rejecting Muhammad's arguments that her agreements to arbitrate are unconscionable.

Muhammad sought and was granted leave to appeal to the Superior Court, Appellate Division. The Appellate Division affirmed, rejecting Muhammad's arguments that the arbitration provision and the class action prohibition are unconscionable. It also concluded that Muhammad's criticisms of the National Arbitration Forum's (NAF) dispute-resolution procedures lacked merit. *Id.* at 241-44.

Judge Kestin concurred in the result, explaining that because County Bank had offered to make the American Arbitration Association available as. a forum for Muhammad to pursue her claims, he would not have "consider[ed] any of plaintiff'sarguments addressed to the validity of NAF's arbitration procedures." *Id.* at 249.

This Court granted Muhammad's motion for leave to appeal. 185 *N.J.* 254 (2005).

LEGAL ARGUMENT

Muhammad's challenges to the enforcement of her arbitration agreements are imbued with the hostility towards arbitration that the Federal Arbitration Act was enacted eight decades ago to nullify. Not only do her arguments give short shrift to the federal and New Jersey policies favoring arbitration; they also inappropriately invoke her merits arguments (wholly unrelated to arbitration) to distract this Court from those policies and the resultant necessity of enforcing arbitration agreements.

Rather than duplicating County Bank's arguments, in this brief we make several related but distinct points to demonstrate to this Court why the decision of the Appellate Division was correct, and why requiring these parties to arbitrate is important to the business community generally.

I. AN AGREEMENT TO ARBITRATE ON AN INDIVIDUAL BASIS CANNOT BE DEEMED UNENFORCEABLE MERELY BECAUSE THE UNDERLYING CONTRACT PROHIBITS CLASS ACTIONS.

Muhammad asks this Court to declare the prohibition against class actions in her loan agreements unconscionable and thereby nullify her agreement to arbitrate individually. Her arguments are premised on a fundamental misconception that, because the doctrine of unconscionability is generally applicable to all contracts, an arbitration agreement may be voided by the simple expedient of making an *ad hoc* determination that one of its provisions is "unconscionable."In fact, the FAA cannot be circumvented so easily.

In enacting the FAA, Congress "declared a national policy favoring arbitration and withdrew the power of the

states to require a judicial forum for the resolution of claims which the contracting parties agreed to resolve by arbitration." *Southland Corp. v. Keating,* 465 *U.S. 1,* 10, 104 S. Ct. 852, 858, *79 L.Ed.2d 1, 12* (1984). The Act's "basic purpose" is "to put arbitration provisions on the same footing' as a contract's other terms." *Allied-Bruce Terminix Cos. v. Dobson,* 513 *U.S.* 265, 275, 115 S. Ct. 834, 840, 130 *L.Ed.2d* 753, 765 (1995) (quoting *Scherk v. Alberto-Culver Co.,* 417 *U.S.* 506, 511, 94 S. Ct. 2449, 2453, 41 *L.Ed.2d* 270, 276 (1974)). *See also Martindale v. Sandvik, Inc.,* 173 *N.J. 76,* 83-84 (2002) ("Congress enacted the Federal Arbitration Act * * * to abrogate the then-existing common law rule disfavoring arbitration agreements `and to place arbitration agreements upon the same footing as other contracts.,") (quoting *Gilmer V. Interstate/Johnson Lane Corp.,* 500 *U.S. 20, 24,* 111 S. Ct. 1647, 1651, 114 *L.Ed.2d* 26, 36 (1991)).

Accordingly, Section 2 of the FAA "embodies a clear federal policy of requiring arbitration unless the agreement to arbitrate * * is revocable `upon such grounds as exist at law or in equity for the revocation of any contract.'" *PerryThomas,* 482 *U.S.* 483, 489, 107 S. Ct. 2520, 2525, 96 *L.Ed.2d* 426, 435 (1987) (quoting 9 *U.S.C. § 2).* Unless that savings clause applies, "[a]n agreement to arbitrate is valid, irrevocable, and enforceable, *as a matter of federal law." Id.* at 492 n.9 (emphasis in original) (citation omitted).

Thus, section 2 of the FAA carves out a limited role for the states in the regulation of contractual arbitration. An agreement to arbitrate may be invalidated on state-law grounds only "if that law arose to govern issues concerning the validity, revocability, and enforceability of contracts generally." *Perry,* 482 *U.S.* at 492 n.9 (emphasis in original). Accordingly, Section 2 gives the states, for example, "a method for protecting consumers against unfair pressure to agree to a contract with an unwanted arbitration provision."

Allied-Bruce, 513 *U.S.* at 281. However, "[a] state-law principle that takes its meaning precisely from the fact that a contract to arbitrate is at issue does not comport with this requirement of § 2." *Perry,* 482 U.S. at 493 n.9 (citation omitted). "Nor may a court rely on the uniqueness of an agreement to arbitrate as a basis for a state-law holding that enforcement would be unconscionable, for this would enable the court to effect what * * * the state legislature cannot." *Id.*

In sum, as the Supreme Court has ruled:

> What States may not do is decide that a contract is fair enough to enforce all its basic terms (price, service, credit), but not fair enough to enforce its arbitration clause. The Act makes any such state policy unlawful, for that kind of policy would place arbitration clauses on an unequal "footing," directly contrary to the Act's language and Congress' intent.

Allied-Bruce, 513 *U.S.* at 281. *See also Martindale,* 173 *N.J.* at86 (quoting *Allied-Bruce).*

The *ad hoc* creation of unconscionability doctrine in order to defeat arbitration is impermissible under any circumstances. But in this case it is particularly uncalled for because the prohibition on class actions in the contracts between Muhammad and County Bank is not contained within the arbitration provisions. Instead, it is a separate, free-standing provision. Pa 186-88. Accordingly, we agree with County Bank that whether the class-action prohibition is enforceable is not a "gateway" question of arbitrability for a court *(see Howsam v. Dean Witter Reynolds, Inc.,* 537 *U. S. 79,* 84, 123 S. Ct. 588, 592, 154 *L. Ed. 2d* 491, 497 (2002)); rather, it is reserved for the arbitrator. *Prima* Paint *v. Flood & Conklin Manufacturing Co.,* 388 *U.S.* 395, 402-04, 87 S. Ct. 18011 1805-06, 18 *L.E.2d* 1270, 1276-77 (1967). *See generally* County Bank Br. 31-34.

Even if the Court were to reach the issue, however, it would be inappropriate to deny enforcement of Muhammad's arbitration agreement on the ground that her underlying contract contains a class-action waiver. Under the existing law of this state, the inclusion of such a waiver in a contract is not unconscionable. Moreover, any newly-minted principle of New Jersey law that invalidates waivers of class arbitration would be preempted by the FAA.

A. Under Either New Jersey or Delaware: Law, Class-Action Waivers Are Not Unconscionable.

Muhammad challenges the class-action waivers in her contracts as unconscionable under New Jersey law. See Muhammad Br. 16-24. Her arguments in this case are a particularly clear example of the burgeoning strategy of seeking the invalidation of arbitration agreements based on state-law rules that are described under the rubric of general contract law, but in fact have been fashioned solely to deal with arbitration agreements. However, there is no place for her arguments either in the law of this state or under Delaware law.

1. Under New Jersey law, class-arbitration waivers are enforceable.

Courts are (and should be) sparing in their reliance on the doctrine of unconscionability to invalidate contractual agreements. In accordance with this principle, the standards under New Jersey law for a finding of unconscionability are stringent.[1] As one appellate court has explained, to

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[1] As the Appellate Division noted, courts in New Jersey (as in many other states) examine unconscionability by looking "at two factors, namely, unfairness in the formation of the contract (procedural unconscionability) and excessively disproportionate terms (substantive unconscionability)." *Muhammad*, 379 *N.J. Super.* at 236 (citing *Sitogum*

"demonstrate unconscionability," a plaintiff must "show[] some overreaching or imposition resulting from a bargaining disparity between the parties, or such patent unfairness in the contract that ***no reasonable person*** not acting under compulsion or out of necessity would accept its terms." *Howard v. Diolosa,* 241 *N.J. Super.* 222, 230 (App. Div. 1990) (emphasis added). See also *Sitogum,* 352 *N.J. Super.* at 565 (contract is substantively unconscionable only if it is "so one-sided as to **shock the *court's conscience")*** (emphasis added).

Given the strict nature of New Jersey's unconscionability standard, it is no surprise, then, that the leading New Jersey appellate decision on the issue has concluded that class-action waivers in arbitration provisions are fully enforceable. See *Gras v.* Assocs. *First* Capital *Corp., 346 N.J. Super.* 42, 54 (App. Div. 2001). In *Gras,* the plaintiffs argued (as Muhammad does here) that an "arbitration agreement's preclusion of their right to proceed as a class * * * violates New Jersey's policy of protecting consumers." *Id.* at 49. Canvassing case law from around the country, the Appellate Division noted some of the many cases that have found class-action waivers to be enforceable. Id. at 49-51. As to those cases "where courts have found arbitration agreements precluding a class action to be unenforceable because of their detrimental impact on consumers' rights" *(id.* at 51), the court's conclusion was straightforward: "These cases are not persuasive." *Id.* Finally, the court held that nothing about the Consumer Fraud Act ("CFA") precluded parties to an arbitration agreement from agreeing to arbitrate CFA claims on an individual basis. Id. at 53-54. *See also Cunningham v. Citigroup, Inc.,* 2005 *WL* 3454312, at *6 (D. N.J. Dec. 16, 2005) ("anti-class action provisions have not been found to

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Holdings, Inc. v. Ropes, 352 *N.J. Super.* 555, 564 (Ch. Div. 2002)). We focus here on the issue of substantive unconscionability.

be per se contrary to public policy under New Jersey state law") (citing *Gras* and decision below).

Gras, Cunningham and the decision below are consistent with the decisions of the overwhelming majority of courts around the country that have addressed the question and declared that a class-action waiver, standing by itself, is not substantively unconscionable.

To begin with, the U.S. Supreme Court broached the issue in *Gilmer v.* Interstate/Johnson *Lane Corp., supra.* The plaintiff. there contended that disputes under the Age Discrimination in Employment Act ("ADEA") should not be subject to arbitration because, among other things, arbitration procedures "do not provide for * * * class actions." 500 *U.S.* at 32. The SupremeCourt rejected that argument, explaining that, "even if the arbitration could not go forward as a class action or class relief could not be granted by the arbitrator, the fact that the [ADEA] provides for the possibility of bringing a collective action does not mean that individual attempts at conciliation were intended to be barred." *Id.* (quotation marks and citation omitted; alteration in original).

Numerous other courts have upheld arbitration provisions that included a prohibition on class actions. As the U.S. Court of Appeals for the Seventh Circuit has explained, "[w]hen contracting parties stipulate that disputes will be submitted to arbitration, they relinquish the right to certain procedural niceties which are normally associated with a formal trial.* * * One of those * * * is the possibility of pursuing a class action." *Champ v. Siegel Trading Co.,* 55 *F.3d* 269, 276 (7th Cir. 1995) (quotation marks and citation omitted). This is perfectly acceptable because the right to a class action is "merely a procedural one, * * * that may be waived." *Johnson v. W. Suburban* Bank, 225 *F.3d* 366, 369 (3d Cir. 2000).

The list of other cases upholding class-action waivers against state-law unconscionability challenges is long and growing by the day. See, e.g., Caley v. *Gulfstream Aerospace Corp., 428 F.3d* 1359, 1378 (11th Cir. 2005) (Georgia law); *Jenkins v. First* Am. Cash Advance *of Ga., LLC,* 400 *F.3d* 868, 877-78 (11th Cir. 2005) (Georgia law); *Iberia Credit Bureau, Inc. v. Cingular Wireless LLC,* 379 *F.3d* 159, 174-75 (5th Cir. 2004) (Louisiana law); *Snowden v. CheckPoint* Check *Cashing,* 290 *F.3d* 631, 638 (4th Cir. 2002) (Maryland law); *Lloyd v.* MBNA Am. Bank, N.A. *27 Fed. Appx. 82, 84* (3d Cir. 2002) (Delaware law); *Provencher v. Dell, Inc.,* _ *F. Supp. 2d* 2006 *WL* 9626, at*5-*7 (C.D. Cal. Jan. 3, 2006) (Texas law); *Dambrosio v. ComcastCorp.,* 2005 *WL* 3543794, at *17 (E.D. Pa. Dec. 27, 2005) (Pennsylvania and Illinois law); *Copeland v. Katz,* 2005 *WL* 3163296, at *4 (E.D. Mich. Nov. 28, 2005) (Michigan law); *Edwards v. Blockbuster, Inc.,* 400 F. *Supp. 2d* 1305, 1309 (E.D. Okla. 2005) (Oklahoma law); *Lux v. Good Guys,* 2005 *WL* 1713421 (C.D. Cal. July 11, 2005) (Nevada law); *In re Currency Conversion* Antitrust *Litig.,* 361 F. *Supp.* 2d 237, 259 & n.ll(S.D.N.Y. 2005) (Arizona, Delaware, Nevada, New Hampshire, and South Dakota law); *Jones v. Genus Credit Mgmt. Corp.,* 353 *F. Supp.* 2d 598, 603 (D. Md. 2005) (Maryland law); *Billups v. Bankfirst,* 294 F. *Supp.* 2d 1265, 1273-77 (M.D. Ala. 2003) (Alabama law); *O'Quin v. Verizon Wireless,* 256 F. *Supp.* 2d 512, 517 (M.D. La. 2003) (Louisiana law); *Lomax v.* Woodmen *of the World Life Ins. Soc'y,* 228 F. *Supp.* 2d 1360, 1365 (N.D. Ga. 2002) (Georgia law); *Vigil v. Sears Nat'l* Bank, 205 *F. Supp. 2d* 566, 572 (E.D. La. 2002) (Arizona law); *Pick v. Discover Fin. Servs., Inc.,* 2001 *U.S.* Dist. *LEXIS* 15777, at *16 (D. Del. Sept. 28, 2001) (Delaware law); Zawikowski v. *Beneficial Nat'l* Bank, 1999 *U.S. Dist. LEXIS* 514, at *5 (N.D. Ill. Jan. 11, 1999) (Illinois law); *Rains v. Found. Health Sys. Life* & Health, 23 *P.3d* 1249, 1253 (Colo. Ct. App. 2001) (Colorado law); *Brown v. KFC Nat'l Mgmt Co.,* 921 P.2d 146, 166-67 & n.23 (Haw. 1996) (Hawaii law);

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[2] *But see, e.g., Discover* Bank v. *Superior Court*, 113 *P.3d* 1100 (Cal. 2005) (determining that in "some circumstances" class action waivers in arbitration provisions are unconscionable); State *ex rel. Dunlap v. Berger*, 567 *S.E.2d* 265, 279-81 (W. Va. 2002); *Leonard v. Terminix Intl Co.*, 854 So. *2d* 529 (Ala. 2002). The U.S. District Court for the Northern District of West Virginia recently refused to follow *Berger* on the ground that its analysis is preempted by the FAA. See Schultz v. *AT&T Wireless Serrs., Inc.*, 376 F. *Supp.* 2d 685, 691 (N.D. W. Va. 2005). Meanwhile, numerous federal district courts in Alabama have distinguished *Leonard* and enforced class-action waivers under Alabama law on the ground that the arbitration fees in Leonard were far greater than any potential recovery and that the arbitration provision in *Leonard* limited the types of damages that could be awarded and in particular precluded the award of attorneys' fees. *See, e.g., Pitchford v.* AmSouth Bank, 285 F. *Supp.* 2d 1286, 1296 (M.D. Ala. 2003) ("The costs of arbitrating the Leonards' claim (at least [$1,1001) exceeded the dollar value of their claim (less than [$5001), which effectively made arbitration an illusory forum for vindicating their substantive rights."); *Taylor v. First N.* Am. *Nat'l* Bank, 325 *F. Supp. 2d* 1304, 1319-22 (M.D. Ala. 2004)); Battels v. *Sears Nat'l* Bank, 365 *F. Supp. 2d* 1205, 1217 (M.D. Ala. 2005); *Lawrence v. Household* Bank (SB), N.A., 343 F. *Supp.* 2d 1101, 1112 (M.D. Ala. 2004); *Billups v. Bankfirst*, 294 F. *Supp. 2d* 1265, 1276-77 (M.D. Ala. 2003); *Gipson v. Cross Country Bank*, 294 F. *Supp. 2d* 1251, 1263-64

That so many courts have held that there is nothing unconscionable about class-arbitration waivers makes perfect sense because class actions, although at times useful, are in no way so fundamental to the vindication of consumer claims as to be unwaivable. For the vast majority of the history of this state and this nation, class actions for money damages did not even exist. Class actions for damages of the type so prevalent today took shape no more than 40 years ago.[3] Such a recent innovation can hardly be deemed so fundamental as to make a contractual waiver of it categorically unconscionable under New Jersey law. Indeed, the *Gras* court recognized as much, explaining that the CFA contains no "legislative mandate or overriding public policy in favor of class actions," whereas compelling public policy favors the enforcement of arbitration provisions. 346 *N.J. Super.* at 54.

In the face of such authority, Muhammad nonetheless argues that the prohibition against class arbitration should be deemed invalid under New Jersey law because, in her view, it is "exculpatory." See Muhammad Br. 1-2, 16-24. The central authority on which she relies is the Appellate Division's decision in *Lucier v. Williams,* 366 *N.J. Super.* 485 (App. Div. 2004). *See also* Legal Servs. Amicus Br. 2

(M.D. Ala. 2003); *Taylor v. Citibank USA, N.A., 292 F. Supp. 2d* 1333, 1345-46 (M.D. Ala. 2003).

[3] "[M]odern class action practice emerged in the 1966 revision of [Federal Rule of Civil Procedure] 23" *(Ortiz v. Fibreboard Corp., 527 U.S.* 815, 833, 119 S. Ct. 2295, 2308, 144 *L.Ed.2d* 715, 731-32 (1999)), which gave federal-court class actions their "current shape" (Amchem *Prods., Inc. v. Windsor,* 521 *U.S.* 591, 613, 117 S. Ct. 2231, 2245, 138 *L.Ed.2d* 689, 706 (1997)). Revised Rule 23's "most adventuresome innovation" was its authorization of "class actions for damages designed to secure judgments binding all class members save those who.affirmatively elected to be excluded." *Id.* at 614-15. The rule governing modern class actions in New Jersey state courts is of even more recent vintage; Rule 4:32-1 "is modeled after" Federal Rule 23 *(In re Cadillac V-8-6-4 Class* Action, 93 *N.J.* 412, 42425 (1983)).

(citing *Lucier).* But contrary to her implication, *Lucier* does not hold that a consumer's contractual waiver of the class-action device immunizes the business with which she has contracted from liability. *See* Muhammad Br. 16. In *Lucier,* a contract between a home inspection service and home buyers placed a ceiling on the amount of damages recoverable by the buyers, limiting the damages to the lesser of $500 or half the home inspection fee. 366 *N.J. Super.* at 493. Because of that substantive limitation, the Appellate Division held, "the potential damage level is so nominal that it has the practical effect of avoiding almost all responsibility for the professional's negligence." *Id.* By contrast, a prohibition of class actions does not in itself exculpate anyone; a plaintiff would be able to obtain the full measure of damages through individual arbitration.

Nor does the recognition of courts that class actions can be useful in certain cases translate into a general principle of New Jersey law that waivers of the right to proceed on behalf of a class are unenforceable. Muhammad cites a number of cases that point out that class certification may be warranted where individual ***litigation*** of claims is not feasible (Muhammad Br. 17-10; see also Legal Servs. *Amicus* Br. 13-22), but her reliance on those cases misses the mark.[4] None of these cases involved arbitration; instead, courts faced the binary choice between class litigation and individual litigation. A third route individual arbitration - was not presented, and the strong federal policy favoring

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[4] For example, Muhammad cites *Carnegie V. Household International, Inc.,* 376 F.3d 656 (7th Cir. 2004). There, the Seventh Circuit affirmed an order granting class certification explaining that "a class action has to be unwieldy indeed before it can be pronounced an inferior alternative * * * to ***no litigation at all.***" Id. at 661 (emphasis added). Muhammad also cites *Weiss v. Regal Collections,* 385 F.3d 337 (3d Cir. 2004). In that transparently irrelevant case, the Third Circuit held that an offer of judgment under Federal Rule of Civil Procedure 68 to a named plaintiff in a putative class action did not moot the plaintiff's class action complaint under the Fair Debt Collection Practices Act. *Id.* at 348.

arbitration was therefore not at issue. Because of the "simplicity, informality, and expedition of arbitration" *(Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc.*, 473 *U.S.* 614, 628, 105 S. Ct. 3346, 3354, 87 *L.Ed.2d* 444, 456 (1985)), individual ***arbitration*** is far more realistic and accessible than individual ***litigation.*** Indeed, the U.S. Supreme Court has strongly suggested that arbitration is a superior method for consumers to resolve small claims. As the Court explained in *Allied-Bruce,* without the availability of arbitration, "the typical consumer who has only a small damages claim (who seeks, say, the value of only a defective refrigerator or television set)" would be left "without any remedy but a court remedy, the costs and delays of which could eat up the value of an eventual small recovery." 513 *U.S.* at 281. In contrast - as a substantial majority of courts that have considered the issue have concluded - consumers can effectively vindicate small claims through individual arbitration.[5] Accordingly, this Court should reject Muhammad's invitation to devise a novel principle of New Jersey unconscionability law declaring waivers of class arbitration to be unenforceable.

2. Class-arbitration waivers are also enforceable under Delaware law.

We agree with County Bank's contention that Delaware law in fact applies to this case, so we will not repeat the argument. Under the law of that state, too, it is clear that class-arbitration waivers are fully enforceable.

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[5] In addition to decisions of this Court, plaintiffs rely on decisions of the U.S. Supreme Court and Third and Seventh Circuits for their encomium to class actions. See Muhammad Br. 18-19. But the Supreme Court has suggested in *Gilmer* that there is nothing problematic about class-action waivers, and the Third and Seventh Circuits have ruled that class-action waivers in arbitration provisions are enforceable. *See Johnson v. W. Suburban Bank,* 225 *F.3d* 366; *Champ v. Siegel Trading Co.*, 55 *F.3d* 269.

Courts within and outside Delaware have repeatedly concluded that Delaware law does not render the waiver of class arbitration unconscionable. *See, e.g., Edelist v. MBNA* America Bank, '790 A.2d 1249, 1260-61 (Del. Super. Ct. 2001); *Lloyd v. MBNA Am. Bank, N.A.* 27 Fed. *Appx.* 82, 84 (3d Cir. 2002); *Pick v. Discover Fin. Servs., Inc.*, 2001 *U.S. Dist. LEXIS* 15777, at *16 (D. Del. Sept. 28, 2001); *In re Currency Conversion* Antitrust *Litig.*, 361 *F. Supp.* 2d 237, 259 & n.ll (S.D.N.Y. 2005).

In *Edelist,* for example, the Delaware Superior Court upheld a provision of a credit card agreement "preventing arbitration of disputes on a class-wide basis"; noting that the "surrender of that class action right was clearly articulated in the arbitration amendment," the Court saw "nothing unconscionable about it. 790 A.2d at 1260-61. And just last month, two California courts cited *Edelist* in reaching the conclusion that "Delaware would not invalidate an arbitration clause merely because it prohibited class actions."[6]

Thus, if the Court chooses to apply Delaware law (as it should), the class-action waiver in Muhammad's agreements must be upheld - just as it should be under New Jersey law.

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[6] *Klussman v. Cross Country* Bank, 36 Cal. *Rptr.* 3d 728, 735 (Cal. Ct. App. 2005) (citing *Edelist,* but choosing to apply California law instead to invalidate an arbitration provision); *see also Discover Bank v. Superior Court,* 36 Cal. Rptr. 3d 456, 459-60 (Cal. Ct. App. 2005) (on remand from California Supreme Court's decision in *Discover Bank,* 113 *P.3d* 1100, applying Delaware law and holding that "the class action waiver in (plaintiff's) cardholder agreement is enforceable, and not unconscionable, under Delaware law").

B. The FAA Would Preempt A Rule That Class-Arbitration Waivers In Arbitration Agreements Are Unconscionable.

As we explained above (at 10-21), class-action waivers arenot unconscionable under either New Jersey or Delaware law. In any event, the FAA would preempt any state-law holding that it is unconscionable to include in a contract a provision requiringindividual arbitration.

1. Section 2 of the FAA would expressly preempt any holding that prohibitions against class arbitration are unconscionable.

Under Section 2 of the FAA,

> [a]n agreement to arbitrate is valid, irrevocable, and enforceable, *as a matter of federal law,* "save upon such grounds as exist at law or in equity for the revocation of any contract." * * * A state-law principle that takes its meaning precisely from the fact that a contract to arbitrate is at issue does not comport with this requirement of § 2.

Perry, 482 *U.S.* at 492-93 n.9 (citation omitted; emphasis in original) (quoting 9 U.S.C. § 2). Thus, agreements to arbitrate may be invalidated on state-law grounds only "if that law arose to govern issues concerning the validity, revocability, and enforceability of contracts generally." *Id.* (emphasis in original).

That principle does not simply prohibit the invalidation of "arbitration agreements under state laws applicable *only* to arbitration provisions." *Doctor's Assocs., Inc. v.* Casarotto, 517 *U.S.* 681, 687, 116 S. Ct. 1652, 1656,

134 *L.Ed.2d* 902, 909 (1986) (emphasis in original). It also bars courts from impeding the enforceability of arbitration agreements by fashioning rules that invoke broad concepts of contract law but in fact apply only or predominantly to the arbitration setting. As the Fifth Circuit recently explained:

> That a state decision employs a general principle of contract law, such as unconscionability, is not always sufficient to ensure that the state-law rule is valid under the FAA. * * * [S] tate courts are not permitted to employ those general doctrines in ways that subject arbitration clauses to special scrutiny.

Iberia, 379 *F.3d* at 167.

Nor, despite Muhammad's exhortation to do so, could the Court manufacture new principles in the context of thwarting an arbitration agreement. To put it bluntly, "no state can apply to arbitration (when governed by the Federal Arbitration Act) any novel rule." *Oblix, Inc. v. Winiecki,* 374 *F.3d* 488, 492 (7th Cir. 2004). *See* also *Zuver v.* Airtouch *Communications, Inc.,* 103 *P.3d* 753, 759 (Wash. 2004) ("courts may not refuse to enforce arbitration agreements under state laws which apply only to such agreements, or by relying on the *uniqueness* of an agreement to arbitrate") (quotation marks, alterations, and citations omitted; emphasis in original).

To accept Muhammad's invitation to declare County Bank's arbitration provision unconscionable because the underlying contract prohibits class arbitration would run afoul of these rules and thus would be expressly preempted by Section 2 of the FAA.

First, New Jersey has no ***generally applicable*** prohibition against contractual waivers of class actions. Neither Muhammad nor the *amici* supporting her have

pointed to any authority for the proposition that class-action waivers are generally unenforceable under New Jersey law outside the context of arbitration.[7] Absent such case law or statutory authority, the FAA does not permit the creation of such a rule specifically in the context of arbitration. In essence, what Muhammad is asking the Court to do is to declare a ***new*** principle of unconscionability and then to apply it in the very same case to strike down an arbitration provision. That request for the ad *hoc* creation of unconscionability doctrine is inconsistent with the Supreme Court's admonition that state-law contract defenses may be used to void arbitration provisions only if they "arose to govern issues concerning the validity, revocability, and enforceability of contracts ***generally"*** *(Perry,* 482 *U.S.* at 493 n.9 (emphasis added)). Indeed, Congress's rationale for authorizing contract-law exceptions to the general rule that arbitration provisions are enforceable - that there can be no impermissible animosity toward arbitration when a court is merely applying an ***extant,*** generally applicable contract-law defense - loses all force when, as here, the party seeking to avoid arbitration is trying to reinvent and enlarge unconscionability doctrine as it goes along. *See Oblix,* 374 *F.3d* at 492 ("[N]o state can apply to arbitration (when governed by the Federal Arbitration Act) any novel rule.").

Second, as noted above (at 11), the ***generally applicable*** standard for finding unconscionability in New Jersey is a strict one. Under that standard, a plaintiff must "show[] some overreaching or imposition resulting from a bargaining disparity between the parties, or such patent unfairness in the contract that no reasonable person not acting under compulsion or out of necessity would accept its

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[7] In fact, as we noted above, the leading New Jersey appellate decision on the issue has concluded that class-action waivers in arbitration provisions are fully enforceable. *See Gras, supra,* 346 *N.J. Super.* at 54; *see also Cunningham, supra,* 2005 *WL* 3454312, at *6 (citing *Gras* and decision below).

terms." *Howard*, 241 *N.J. Super.* at 230. Put another way, a contract is unconscionable only if it is "so one-sided as to shock the court's conscience." *Sitogum*, 352 *N.J. Super.* at 565.

We submit that it is impossible to conclude that it shocks the conscience, or that one must be acting "under compulsion," to accept a fully disclosed class-action waiver.[8] To the contrary, there are many reasons why a reasonable person would accept a contract that allows for the easy resolution of her own actual, concrete disputes via individual arbitration, but deprives her of the ability to bring class actions for other customers' benefit. Foremost among them is that individual arbitration is the least expensive means of dispute resolution and hence serves to moderate the cost of goods and services (such as the interest rate and fees associated with the loans at issue here).[9] *See Carnival Cruise Lines, Inc. v. Shute*, 499 *U.S.* 585, 594, 111 S. Ct. 1522, 1527, 113 *L.Ed.2d* 622, 632 (1991) (explaining that limiting fora in which cruise line may be sued leads to reduced fares for passengers); *see also* Stephen J. Ware, *Paying the Price of Process: Judicial Regulation of Consumer Arbitration Agreements*, 2001 J. DISP. RESOL. 89, 94 (arguing that class arbitration makes consumers worse

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[8] As the Appellate Division found here, the fact that Muhammad "needed money to purchase school books" did not make her the "victim of sufficient economic duress" to render the arbitration provision unconscionable, though she "may have been experiencing financial stress." *Muhammad*, 379 *N.J. Super* at 241.

[9] We do not dispute that the cost of short-term loans can be high when expressed in annualized percentage terms (as opposed to absolute dollar amounts). Yet they would be higher still in the absence of a prohibition against class actions. Without a class waiver, the high-stakes nature of class arbitration would result in substantially higher litigation costs to lenders; those costs, in turn, would be passed along to borrowers in the form of higher rates or loan fees. At some point, the cost would exceed the means of some borrowers, potentially forcing them to turn to less savory sources of short-term funds.

off by increasing the cost of doing business and, as a result, raises prices for consumers). As the Seventh Circuit has recognized,"[a]rbitration offers cost-saving benefits and `thesebenefits are reflected in a lower cost of doing business that in competition are passed along to customers.'" *Boomer v. AT&T Corp.*, 309 F.3d 404, 419 n.7 (7th Cir. 2002) (quoting *Metro East Ctr. for conditioning & Health v. Qwest Communications Int'l, Inc.*, 294 *F.3d* 924, 927 (7th Cir. 2002) (Easterbrook, J.)).

Individuals may also understand that arbitration will provide them with better results. Studies have shown that "consumers are likely to fare better in arbitration, both in terms of the likelihood of success on the merits and the size of the award, than in litigation" and that "parties who participate in arbitration proceedings are generally satisfied, both in terms of the fairness of the process and the equity of the outcome." Joshua Lipshutz, Note, *The Court's Implicit* Roadmap: Charting the Prudent *Course* At *the Juncture of Mandatory Arbitration Agreements and Class Action Lawsuits,* 57 STAN. L. REV. 1677, 1712 (2005) (footnotes omitted). Consumer perceptions match the reality. A recent poll found that "[a]rbitration is widely seen" by participants "as faster (74%), simpler (63%), and cheaper (51%) than going to court." Harris Interactive, Arbitration: *Simpler,* Cheaper, *and Faster* Than *Litigation* (Apr. 2005), at 5, available at http://www.instituteforlegalreform.org/resources/ArbitrationStudyFinal.pdf.

Moreover, many Americans have become skeptical of classactions. A March 2003 survey found that 1167% of Americans believe that lawyers benefit most from the current class action suit system while 61% think that ***consumers*** (32%) and ***class members*** (29%) benefit ***least*** from the current system." Penn, Schoen & Berland Associates, U.S. Chamber of Commerce, Institute for Legal Reform, Polling on The Class Action System: National Results, available at

http://www.instituteforlegalreform.com/resources/classaction .pdf (emphasis added). These results support the view that "[m]any ordinary Americans seem to think that class actions are a new-fangled litigation device invented by greedy plaintiff attorneys." Deborah R. Hensler, *Revisiting the Monster: New Myths and Realities of Class Action and Other Large Scale Litigation,* 11 DUKE J. COMP. & INTEL L. 179, 180 (2001) . As Congress has recently recognized,' "abuses of the class action device" have "undermined public respect" for the judicial system, and created a system in which "[c]lass members often receive little or no benefit from class actions, and are sometimes harmed," while lawyers generate large fees. Class Action Fairness Act of 2005, Pub. L. 109-2, § 2 (codified at 28 *U.S.C.* § 1711 note).

Accordingly, a consumer would not be irrational in the least to trade the ability to be part of a class action for the availability of arbitral dispute resolution, particularly because individual arbitration generally leads to reduced dispute-resolution costs for consumers.[10] To assume otherwise would contravene New Jersey's ***generally applicable*** approach to unconscionability, which Section 2 of the FAA forbids. "Even when using doctrines of general applicability, the state courts are not permitted to employ those general doctrines in ways that subject arbitration clauses to special scrutiny." *Iberia,* 379 *F.3d* at 167.

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[10] Of course, the consumer could also rationally choose to trade the ability to be part of a class action in consideration for other benefits furnished as part of the underlying contract, such as ready access to short-term, unsecured credit.

2. Conditioning the enforceability of arbitration provisions on the availability of class-wide arbitration would conflict with Congress's objectives in enacting the FAA and would therefore be preempted.

Any holding that an arbitration provision must allow for class-wide arbitration in order to be enforceable is also preempted under traditional principles of conflict preemption because it "stands as an obstacle to the accomplishment and execution of the full purposes and objective of Congress" in enacting the FAA. *United States v. Locke,* 529 *U.S.* 89, 109, 120 *S. Ct.* 1135, 1148, 146 *L.Ed.2d* 69, 89 (2000) (internal quotation marks and citation omitted).

Section 2 of the FAA declares pre-dispute arbitration agreements "valid, irrevocable, and enforceable" because "arbitration saves time, saves trouble, saves money." *Joint Hearings* on S. *1005 and H.R. 646 Before* the Subcomms. *of the Comms. on the Judiciary,* 68th Cong., 1st Sess., at 7 (1924) (statement of Charles Bernheimer, N.Y. Chamber of Commerce). As Congress later explained, arbitration usually is "cheaper and faster than litigation," has "simpler procedural and evidentiary rules," "minimizes hostility," and is "more flexible in regard to scheduling." H.R. REP. No. 97-542, at 13 (1982). The U. S. Supreme Court, too, has recognized the superior "simplicity, informality, and expedition of arbitration." *Mitsubishi,* 473 *U.S.* at 628. *See also Barcon Assocs., Inc. v. Tri-County Asphalt Corp.,* 86 *N.J.* 179, 187 (1981) (arbitration's "object is the final disposition, in a speedy, inexpensive, expeditious and perhaps less formal manner, of the controversial differences between the parties") (citation and quotation marks omitted).

Class-action procedures, by contrast, are antithetical to the low-cost and efficient resolution of disputes that is the

hallmark of arbitration. While the average length of an AAA arbitration from filing to award is less than six months *(see Allied-Bruce,* 513 *U.S.* at 280-81), class actions can take years. These complex matters invariably begin with a lengthy collateral proceeding to determine the propriety of class certification, which generally entails (i) substantial discovery, including depositions of all class representatives (and often other witnesses) for purposes of determining such statutory prerequisites as typicality and adequacy of the class representatives and commonality of the claims across class members; (ii) plenary briefing of the class certification issue; (iii) an evidentiary hearing; (iv) a written ruling; and very often (v) a motion for leave to appeal initiated by the losing party; and, if leave is granted, (vi) the subsequent, fully-briefed interlocutory appeal.

If, after all of that, a class is certified, there would have to be full and adequate notice to class members and an opportunity to opt out. Discovery commensurate with the now-increased stakes of the litigation would then begin and likely continue for years. Should the defendant then yield to the hydraulic pressure to settle that class certification creates, there would need to be another round of notice followed by a fairness hearing, complete with extensive briefing by both sides and by any objectors. And. if the defendant chooses not to settle, there would need to be a class-wide trial - one in which the plaintiffs are required to establish any individualized elements of their claims and the defendant is afforded the opportunity to put on any individualized defenses.

Whether conducted by a court or by an arbitrator, all of the procedures necessary to the fair administration of a class action make arbitration more expensive and more time consuming – and, in the process, eradicate the distinction

between arbitration and litigation.[11] In fact, some commentators believe that "class arbitration may actually prove **more** burdensome than class litigation." Jack Wilson, *"No-Class-Action Arbitration Clauses," State-Law Unconscionability, and the Federal Arbitration Act: A Case for Federal Judicial Restraint and Congressional Action*, 23 QUINNIPIAC L. REV. 737, 774 (2004) (emphasis added) ; *see also* Lindsay R. Androski, *Comment, A Contested Merger: The Intersection of Class Actions and Mandatory Arbitration Clauses*, 2003 U. CHI. LEGAL F. 631, 649 (hybrid class arbitration "subjects arbitration to the very judicial burden that the contracting parties sought to avoid through arbitration").

Not only would grafting time-consuming and expensive class-action procedures onto an arbitral proceeding essentially eliminate the distinction between arbitration and litigation, but it also presents businesses with a "worst-of-all-worlds" scenario. While the stakes would be increased exponentially over an individual arbitration, any

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[11] See Jonathan R. Bunch, Note, *To Be Announced: Silence from the United States Supreme Court and Disagreement Among Lower Courts Suggest an Uncertain Future for Class-Wide Arbitration: Green Tree Fin. Corp. v. Bazzle*, 2004 J. DISP. RESOL. 259, 272 ("[W]hen class-wide arbitration is chosen as the means to resolve many similar claims, the many benefits of the arbitration process are lost in favor of a procedural device which brings the burdens of litigation into the arbitral forum. It is somewhat ironic that the greatest advantages of arbitration are in many instances the greatest disadvantages of litigation, yet class-wide arbitration * * * lessens the distinction between the two processes."); Jean R. Sternlight, As Mandatory *Binding Arbitration Meets the Class Action, Will* the *Class* Action *Survive?*, 42 Wm. & MARY L. REV. 1, 44-45 (2000) ("[S]everal attorneys who have actually participated in classwide arbitrations have found that the procedure, at least as used to date, differs very little from litigation and thus offers few, if any, advantages."); Elizabeth P. Allor, *Note, Keating v. Superior Court: Oppressive Arbitration Clauses in Adhesion Contracts*, 71 CAL. L. REV. 1239, 1253 (1983) ("[W]hen conducted -on a classwide basis, arbitration is unlikely to remain inexpensive and efficient.").

class-wide arbitral award would remain reviewable only for fraud, bias, or "manifest disregard" of the law. See 9 *U.S.C.* § 10; *Wilko v. Swan,* 346 *U.S. 427,* 436-37, 74 S. Ct. 182, 187, 98 *L.Ed.* 168, 176 (1953), *overruled on other grounds by Rodriguez de Quijas V.* Shearson/American *Express, Inc.,* 490 *U.S. 477,* 109 S. Ct. 1917, 104 *L.Ed.2d* 526 (1987). In such circumstances, few businesses would be willing to roll the dice by including an arbitration provision in their consumer contracts; "[c]lass arbitration just seems to present too many risks." Wilson, *supra,* 23 QUINNIPIAC L. REv. at 778.

As the distinction between litigation and arbitration erodes, businesses will stop including arbitration provisions in their contracts in the first place, concluding "that the known, class litigation, is preferable to unknown, class arbitration." *Id.* Thus, the consequence of conditioning the enforcement of consumer arbitration provisions on the business subjecting itself to class-wide arbitration would not be fairer or more efficient arbitration - but rather ***more litigation*** and ***less arbitration.*** Nothing could more clearly "frustrate the purpose" (Livadas v. *Bradshaw,* 512 U.S. 107, 116, 114 *S.* Ct. 2068, 2074, 129 *L.Ed.2d* 93, 105 (1994)) of the FAA. As the Fifth Circuit recently explained in rejecting an attack on a class-arbitration waiver "the fact that certain litigation devices may not be available in arbitration is part and parcel of arbitration's ability to offer `simplicity, informality, and expedition,' characteristics that generally make arbitration an attractive vehicle for the resolution of low-value claims." *Iberia,* 379 *F.3d* at 174 (quoting *Gilmer,* 500 *U.S.* at 31) ; *see also id.* At (for parties to demand "all of the procedural accoutrements that accompany a judicial proceeding" would undermine "the point of arbitration").

Accordingly, under the doctrine of conflict preemption -and regardless of any state-law concern about "the unavailability of class action relief" - "the Supremacy

Clause of the Federal Constitution * * * preclude[s] [a court] from invalidating an arbitration agreement otherwise enforceable under the FAA simply because a plaintiff cannot maintain a class action." *Pyburn v. Bill Heard* Chevrolet, 63 *S.W.3d* 351, 364 (Tenn. Ct. App. 2001), *appeal* denied (Tenn. Nov. 19, 2001). See *also Schultz v. AT&T Wireless Servs., Inc.*, 376 F. *Supp. 2d* 685, 691(West Virginia Supreme Court's holding that class-arbitration waiver was unconscionable is preempted by the FAA and therefore "the plaintiff's argument that the arbitration clause is unconscionable due to its foreclosure of class action relief * * * lacks merit"); *Am. Gen. Life & Accident Ins. Co. v. Wood,* 429 F.3d 83, 90 (4th Cir. 2005) ("West Virginia precedent generally barring state claims from arbitration must be necessarily circumscribed in light of [the FAA]"); *Caley,* 428 *F.3d* 1359, 1378 (arbitration provision's prohibition of class actions is "consistent with the goal of 'simplicity, informality, and expedition' touted by the Supreme Court in Gilmer") (quoting *Gilmer,* 500 *U. S.* at 31).

The strong pro-arbitration purposes of the FAA thus preempt the invention of any state-law principle that would broadly invalidate class-action waivers as applied to arbitration provisions.

II. AN OFFER TO PAY THE COSTS OF ARBITRATION AND TO PROCEED IN AN ALTERNATIVE ARBITRAL FORUM MOOTS ANY ARGUMENT THAT THE COSTS OF ARBITRATION ARE EXCESSIVE OR THAT THE ORIGINAL FORUM IS PROBLEMATIC.

Muhammad argues that she should not be required to arbitrate because she considers the costs of arbitration to be prohibitively expensive. See Muhammad Br. at 22-26. But County Bank long ago offered to pay all of the costs of

arbitration. Muhammad rebuffed that offer, however, so that she could continue to pursue her argument that it is too expensive for her to arbitrate. Allowing her to do so would be entirely unjustified.

To be sure, the U.S. Supreme Court has recognized that, in some circumstances, "the existence of large arbitration costs could preclude a litigant * * * from effectively vindicating her * * * rights in the arbitral forum." *Green Tree Fin. Corp.-Ala. v. Randolph,* 531 *U.S. 79,* 90, 121 S. Ct. 513, 522, 148 *L.Ed.2d* 373, 383 (2000). But the Court made clear that the mere "'risk' that [one] will be saddled with prohibitive costs is too speculative to justify the invalidation of an arbitration agreement" (id. at 91). Nevertheless, plaintiffs routinely invoke such speculation as a stratagem to avoid arbitration. As a result, the Chamber's members often find themselves faced with the argument (whether legitimate or not) that arbitral costs are too high.

In such circumstances, offers to pay the costs of arbitration (such as the one County Bank has made here) are entirely appropriate. As numerous courts around the nation have explained, in order to effectuate the strong federal policy favoring arbitration, offers to pay the costs of arbitration should be credited when considering whether an arbitration provision is enforceable. *See, e.g., Livingston v. Assocs. Fin., Inc.,* 339 F.3d 553, 557 (7th Cir. 2003) ("the fact that [the defendant] agreed to pay *all* costs associated with arbitration forecloses the possibility that the [plaintiffs] could endure any prohibitive costs in the arbitration process") (emphasis in original) ; *Anders v. Hometown Mtg. Servs., Inc.,* 346 F.3d 1024, 1026 (11th Cir. 2003); *Large v. Conseco Fin. Servicing Corp.,* 292 F.3d 49, 56-57 (1st Cir. 2002) ("Conseco's offer to pay the costs of arbitration and to hold the arbitration in the Larges' home state of Rhode Island mooted the issue of arbitration costs.") ; *Dobbins v. Hawk's Enters.,* 198 F.3d 715, 717 (8th Cir. 1999) ; *Anderson v.*

Delta Funding Corp., 316 F. *Supp. 2d* 554, 567 (N.D. Ohio 2004) ; *Jung v. Ass'n of Am. Med. Colts.*, 300 F. *Supp.* 2d 119, 148-49 (D.D.C. 2004) ; *In re Currency Conversion Fee* Antitrust Litig. 265 F. *Supp.* 2d at 41112; *Nelson v. Insignia/ESG, Inc.* 215 *F. Supp. 2d* 143, 157 (D.D.C. 2002); *First Family Fin. Servs., Inc. v. Sanford,* 203 F. *Supp.* 2d 662, 667 (N.D. Miss. 2002) ; *Baugher v. Dekko* Heating *Techs.*, 202 *F. Supp. 2d* 847, 850 (N.D. Ind. 2002) ; *Phillips v. Assocs. Home Equity Servs., Inc.*, 179 F. *Supp. 2d* 840, 847 (N.D. Ill. 2001) ; *Nur v. K.F.C., USA, Inc.*, 142 F. *Supp. 2d* 48, 52 (D.D.C. 2001) ; *Zuver,* 103 P.3d at 763 & n.7 ("refus[ing] to ignore" defendant's "offer[] to `defray the cost of arbitration' by paying arbitration fees," thus rendering "moot" the plaintiff's argument that the fees were unconscionable); *Zobrist v. Verizon Wireless,* 822 *N.E.2d* 531, 539 (Ill. Ct. App. 2004) ("Verizon has already stipulated to a waiver of [the cost-sharing] provision, which, in effect, serves to moot the plaintiff's argument" that arbitration costs are excessive).

Muhammad cites a handful of cases that treat offers to pay the costs of arbitration as unaccepted offers to modify a contract (i.e., the arbitration agreement). See Muhammad Br. 25-26. At bottom, the holding of these cases amounts to a rule that an individual may rely on a contractual term for the sole purpose of seeking to invalidate that contract as unconscionable. That kind of reliance interest lacks legitimacy; in any event, it must fall to the policies favoring arbitration. As the U.S. Supreme Court has explained in a different context, parties resisting enforcement of their arbitration agreements could not avoid arbitration based on the claim "that they agreed to arbitrate future disputes * * * in reliance on [an earlier case] holding that such agreements would be held unenforceable by the courts." *Rodriguez,* 490 *U.S.* at 485. Along similar lines, the Fifth Circuit reversed a lower court's holding that an offer to pay costs constituted an "invalid" unilateral revision to a contract. *Carter v.*

Countrywide Credit Indus., Inc., 362 *F.3d* 294, 300 n.3 (5th Cir. 2004). The court explained that, although that "observation may be accurate as a matter of contract law, what is at issue here is whether these plaintiffs will be required to pay prohibitive arbitration fees and costs if they are forced to proceed to arbitration." *Id.* (emphasis in original). Given an offer to bear all costs, the answer to that question is plainly "no."

The strong federal policy favoring arbitration also supports viewing such offers to pay the costs of arbitration as mooting challenges based on cost. When companies draft standardized arbitration provisions for large numbers of customers, they cannot predict *ex* ante which customers will initiate arbitration with them, what the issues will be in those arbitrations, or what those customers, financial status will be at the time of those disputes. Standardized arbitration provisions nonetheless must allocate arbitration fees between the company and customer in a way that *ex ante* seems reasonable (or, with some frequency, incorporate the default fee schedules of arbitration providers such as the American Arbitration Association or National Arbitration Forum, which Justice Ginsburg has described as providing "models for fair cost and fee allocation." *Randolph*, 531 *U.S.* at 95 (Ginsburg, J., concurring in part and dissenting in part)). Like any ex ante estimate, of course, from time to time the estimated arbitration costs will be more expensive than some customers can reasonably bear (and in other instances will be less expensive than other customers can bear). If the arbitration provision were held unconscionable with respect to every customer who could not afford the costs of arbitration (or claimed he or she could not), that would lead to the widespread invalidation of arbitration provisions. Such a result would run counter to "[t]he preeminent concern of Congress in passing the [FAA]" which "was to enforce private agreements into which parties had entered." *Dean Witter Reynolds, Inc. v. Byrd*, 470 *U.S.* 213, 221, 105 S. Ct.

1238, 1243, 84 *L.Ed.2d* 158, 166 (1985); *see also Moses H. Cone Mem'l Hosp. v. Mercury Constr. Corp.*, 460 *U.S. 1*, 25-261 103 S. Ct. 927, 941, 74 L.Ed.2d 765, 785 (1983) ("any doubts concerning the scope of arbitrable issues should be resolved in favor of arbitration"). Permitting a company to offer to pay arbitration costs alleged to be unaffordable, by contrast, serves the policies favoring arbitration.

Similar considerations also support offers like the one County Bank has made to 'submit to individual arbitration before an alternative forum - the American Arbitration Association. County Bank made that offer after Muhammad indicated in her briefing to the superior court that she believed that her "rights `would be better protected in an arbitration conducted before the AAA as opposed to the [National Arbitration Forum.]'" 379 *N.J. Super.* at 232. For the reasons explained in County Bank's brief, Muhammad's challenges to the NAF, a leading arbitration provider, are meritless.[12] But in any event, as Judge Kestin explained in his concurring opinion below, an offer to make the AAA available as a alternative forum moots the attack on the NAF:

> Because of plaintiff's rejection of defendants' offer to arbitrate the matter under the aegis of the American Arbitration Association * * *, I would not consider any of plaintiff's arguments addressed to the validity of NAF's arbitration procedures. Having forgone the opportunity to avoid the asserted bias and procedural unconscionability inflicted by NAF arbitration

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[12] Many members of the Chamber have entered into arbitration agreements in which the NAF is the selected arbitration provider. As the U.S. District Court for the Central District of California recently remarked in ordering individual arbitration of a consumer claim, "the NAF * * * is without question an inexpensive, efficient, and convenient forum for resolving commercial disputes." *Provencher v. Dell, Inc.*, 2006 WL 9626, at *1.

> standards, plaintiff should not now be heard to attack those very processes, which she, for a second time, elected to be bound by.

379 *N.J. Super.* at 249.

In particular, County Bank's offer moots Muhammad's argument that the discovery available under the NAF rules is inadequate. To be sure, County Bank has shown convincingly that Muhammad has misunderstood the range of discovery available to her under the NAF rules; the Appellate Division correctly concluded that the NAF rules provide for at least as much discovery - if not more - as is available in New Jersey small claims court. *See Muhammad,* 379 *N.J. Super.* at 243; *see also* County Bank Br. 23-25. But even if not, Muhammad's argument is mooted by the bank's offer to arbitrate under the AAA's rules. *See, e.g., Sapiro v. VeriSign,* 310 F. *Supp.* 2d 208, 214 (D.D.C. 2004) ("While defendant maintains that the rules and procedures in the Arbitration Agreement provide for sufficient discovery, [defendant] has agreed to proceed with the arbitration and all discovery under the AAA Rules. * * * Thus, the Court need not determine whether the discovery provisions in the Arbitration Agreement are sufficient."). It would be sheer speculation on Muhammad's part to claim that discovery under the AAA rules is inadequate. As then-Judge Roberts explained for the U.S. Court of Appeals for the D.C. Circuit, the AAA's commercial arbitration rules "leave the decision about which discovery tools to use, and in what manner, to the discretion of the arbitrator." *Booker v. Robert Half Int'l, Inc.*, 413 F.3d 77, 82 (D.C. Cir. 2005). "To invalidate the agreement on the basis of [plaintiff's] speculation would reflect the very sort of suspicion of arbitration the Supreme Court has condemned as far out of step with our current strong endorsement of the federal statutes favoring this method of resolving disputes." *Id.* (internal quotation marks omitted).

* * * * *

If the federal and New Jersey policies favoring the enforcement of arbitration agreements are taken seriously, offers to waive any allegedly problematic features of an arbitration provision must not be cast aside.

III. MUHAMMAD MAY NOT EVADE HER OBLIGATION TO ARBITRATE BY LEVELING A PUBLIC-POLICY ATTACK ON THE UNDERLYING CONTRACT.

Muhammad's back-door challenge to the arbitration agreementon public policy grounds should also be rejected. Muhammad and her *amici* spend pages of their briefing excoriating "payday lending" practices in an effort to convince this Court that it should invoke policy concerns related to such practices to deny enforcement of County Bank's arbitration provision. See Muhammad Br. 13-16; AARP *Amici* Br. 1, 5, 7-28; Legal Servs. *Amicus Br.* 3-10. Indeed, one group of Muhammad's *amici* focuses its entire brief on attacking the entire short-term loan industry, addressing not only alleged present practices but also purported conduct from as far back as 60 years ago. See AARP *Amici* Br. 13-14.[13] But such arguments are wholly irrelevant to the enforceability of a specific arbitration provision in a specific contract.

Concerns about payday lending can and should be directed to the New Jersey State Legislature, United States Congress, and state and federal agencies - all' of which are well-equipped to address them. However, such attacks cannot be used to escape from an agreement to arbitrate

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[13] In their most dramatic claim, *amici* go so far as to suggest that payday lending injures our soldiers (AARP Amici Br. 8-10). That sort of overreaching attack is designed to distract the Court from the narrow legal issue before it - whether an arbitration provision is enforceable.

disputes arising out of a ***specific*** contract. Under the FAA, challenges to the validity of a contract as a whole that contains an arbitration provision are for the arbitrator, not a court, to decide. An arbitration agreement is separable from, and must be considered independently of, the underlying contract. *Prima* Paint, 388 *U.S.* 395, 402-04. As a matter of the "federal substantive law of arbitrability" *(Moses H. Cone,* 460 *U.S.* at 24), the sole focus must be on the ***arbitration*** agreement. The subject matter of the underlying contract is of no legitimate concern to the Court; such merits issues are solely for an arbitrator to consider.[14] Indeed, Muhammad is free to argue to the arbitrator that her entire loan agreement is invalid on public policy grounds. There is no basis to think that an arbitrator cannot make such a determination, as "we are well past the time when judicial suspicion of the desirability of arbitration and of thecompetence of arbitral tribunals inhibited the development of arbitration as an alternative means of dispute resolution." Mitsubishi, 473 *U.S.* at 626-27.

Without trivializing New Jersey's legitimate interests in the area of payday lending - which as discussed above can be addressed by the representative branches of state and federal government - it nonetheless remains the case that the FAA does not permit reliance on such "public policy" grounds to eviscerate the enforceability of arbitration

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[14] Hence, for example, every federal court of appeals to have considered the issue has held that a party cannot avoid an arbitration agreement by challenging the underlying contract as illegal. *See Jenkins,* 400 *F.3d* at 880-82; *Bess v. Check Express,* 294 F.3d 1298, 1304-06 (11th Cir. 2002); *Snowden,* 290 F.3d at 636-38; *Burden v. Check Into Cash of Ky., LLC,* 267 *F.3d* 483, 489-90 (6th Cir. 2001); *Harter v. Iowa Grain Co.,* 220 *F.3d* 544, 550 (7th Cir. 2000) ; *3H & Assocs., Inc. v. Hanjin Eng'g & Constr. Co.,* 1998 *WL* 657722, at *2 (9th Cir. Sept. 3, 1998) (unpublished) ; *Lawrence v. Comprehensive Bus. Servs. Co.,* 833 *F.2d* 1159, 1161-62 (5th Cir. 1987). *But see, e.g., Cardegna v. Buckeye Check Cashing, Inc.,* 894 *So.2d* 860 (Fla.), *cert. granted,* 125 S. Ct. 2937 (2005), argued Nov. 29, 2005.

agreements. *Prima Paint* requires courts to determine arbitrability with reference to the arbitration agreements ***alone***: courts "may consider only issues relating to the making and performance of the agreement to arbitrate." 388 U.S. at 404. On that score, it is clear that, just as under federal law, "New Jersey courts also have favored arbitration as a means of resolving disputes." Martindale, supra, 173 *N.J.* at 84; *see also id.* at 85 (collecting cases).

Hence, Muhammad's attempt to shift attention from the arbitrability of her dispute to policy concerns about payday lending cannot withstand scrutiny under *Prima Paint* and its progeny. The Appellate Division was right to reject it. *See Muhammad,* 379 *N.J. Super.* at 234 ("if the practice of offering payday loans in this State is to be abolished, it will take legislative action to do so.").

IV. THE ENFORCEABILITY OF AN ARBITRATION PROVISION SHOULD NOT BE SUBJECT TO QUESTION MERELY BECAUSE IT HAPPENS TO BE CONTAINED WITHIN A FORM CONTRACT.

Muhammad also expends much effort criticizing her arbitration agreement because it is part of a form contract drafted by a company. See Muhammad Br. 13-16; *see* also Legal Servs. *Amicus* Br. 24-29. Indeed, boiled down to their essence, many of Muhammad's arguments are nothing more than a challenge to the use of form contracts themselves. However, as this Court has explained, "the observation that [a given contract] fit[s] the definition of contracts of adhesion is the beginning, not the end, of the inquiry." *Rudbart v. North Jersey Dist. Water Supply Comm'n,* 127 *N.J.* 344, 354 .(1992). Although it is incumbent on courts to ensure that form contracts - like any other contract - are not used in such a one-sided fashion as to deny consumers their rights, those contracts are critical to the modern economy

and the business of the Chamber's members; generic aspersions on them have no place in the law of this or any other state.

The standardization of contractual terms serves the same values as the standardization of goods and services, and is equally "essential to the functioning of the economy." 1 JOSEPH M. PERILLO, CORBIN ON CONTRACTS (rev. ed. 1993) § 1.4, at 15[15]. Form contracts reduce transaction costs by obviating the need to negotiate and draft a separate agreement for each transaction. Market forces enhance the efficiency of standard-form terms; even form contractual terms that might appear to confer an undue advantage to the drafter benefit consumers ex ante by resulting in lower prices due to the drafter's lower marginal costs. *See Carbajal v. H&R Block Tax Servs., Inc.,* 372 F.3d 903, 906 (7th Cir. 2004) ("[f]orms reduce transactions costs and benefit consumers because, in competition, reductions in the cost of doing business show up as lower prices") ; *see generally* RICHARD A. POSNER, ECONOMIC ANALYSIS OF THE LAW 127-29 (5th ed. 1998) ; Richard Craswell, *Property Rules and Liability Rules in Unconscionability and Related Doctrines,* 60 U. CHI. L. REV. 1, 39-40 (1993) ; Ronald H. Coase, *The Choice of the institutional Framework: A Comment,* 17 J.L. & ECON. 493, 494 (1974).

Indeed, without form contracts, significant portions of the modern economy would come to a complete standstill. Were banks required to negotiate individually with consumers each time a consumer applied for a credit card or

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[15] *See also* John J.A. Burke, *Contracts as a Commodity: A Nonfiction Approach,* 24 SETON HALL LEGIS. J. 285, 290 (2000) (estimating that standard forms account for more than 99 percent of all contracts); Robert W. Gomulkiewicz, *The License Is the Product: Comments on* the *Promise of Article 2B for Software* and *Information Licensing,* 13 BERKELEY TECH. L.J. 891, 895-900 (1998) (noting that standard-form terms make electronic commerce possible).

a mortgage, no one but Bill Gates would ***have*** a credit card or mortgage. Were manufacturers required to negotiate each term in a warranty prior to the sale of an appliance, all televisions would come "as is," without any warranty - or manufacturers would simply stop making televisions. Were cellular telephone providers required to negotiate each term of their contracts on a customer-by-customer basis, there would be no cell phones available for love or money.

Furthermore, even were it the case that some form contracts contain terms that may be insufficiently protective of the rights of consumers, the marketplace is itself more than adequate to correct such abuses. For example, consumer objections to the early-cancellation fees contained in certain cellular telephone contracts has caused several companies to offer plans that may be canceled at any time without a fee (but under which the companies presumably charge more for equipment and/or cellular service). Moreover, even if short-term loans are not available without a requirement that disputes be arbitrated, if enough consumers were to express their desire to have agreements without arbitration provisions, some lender would surely offer it - though, of course, other terms of that no-arbitration loan might differ, as the provider would have to price the loan based on its expected costs, including litigation costs. The marketplace will demonstrate whether consumers are willing to pay higher interest rates or fees in exchange for a loan under which all disputes may be resolved in court or via class-wide arbitration; this Court's intervention is unnecessary to achieve that result.[16]

Accordingly, this Court should clarify that, merely because a business offers a form contract on a uniform basis

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[16] Indeed, any holding that class-arbitration waivers are unenforceable would cause lenders and other businesses to curtail operations in New Jersey to the detriment of consumers who would have fewer choices and incur higher prices.

to all who seek that business's services, such a contract is in no way suspect. Any contrary rule would be disastrous for businesses and consumers.

CONCLUSION

This Court should reemphasize its commitment to the well-established principles of federal and New Jersey law favoring the resolution of disputes through arbitration by clarifying that the arbitration agreements between Muhammad and County Bank are fully enforceable.

Respectfully submitted,

/s/

Andrew B. Joseph
DRINKER BIDDLEE & REATH LLP
A Pennsylvania Limited Liability
Partnership
500 Campus Drive
Florham Park, New Jersey 07932
Telephone: (973) 360-1100

Attorney for the Chamber of Commerce of
the United States of America

OF COUNSEL

MAYER, BROWN, ROWE & MAW LLP
Evan M. Tager (*pro hac vice*)
David M. Gossett (*pro hac vice*)
1909 K Street, NW
Washington, DC 20006
(202) 263-3000

NATIONAL CHAMBER LITIGATION CENTER, INC.
Robin S. Conrad (*pro hac vice*)
Amar D. Sarwal (*pro hac vice*)
1615 H Street, NW
Washington, DC 20062
(202) 463-5337

DATED: January 17, 2006

SUPREME COURT OF NEW JERSEY

NO. 58,430

JALIYAH MUHAMMAD	:	ON APPEAL FROM THE
	:	SUPERIOR COURT OF
	:	NEW JERSEY,
Plaintiff-Appellant	:	APPELLATE DIVISION
	:	
v.	:	DOCKET NO. A-0558-04T3
	:	
COUNTY BANK OF	:	
REHOBOTH BEACH,	:	
DELAWARE; EASY CASH;	:	
TELECASH; and MAIN	:	
STREET CORPORATION	:	
	:	
Defendants-	:	
Respondents	:	
	:	

SAT BELOW:
HON. HOWARD H. KESTIN, PJAD
HON. STEVEN L. LEFELT, JAD
HON. JOSEPH A. FALCONE, JAD

CERTIFICATION OF FILING AND PROOF OF SERVICE

I, the undersigned, hereby certify that on this 17th day of January, 2006, the original and nine (9) copies of an Amicus Brief on behalf of the Chamber of Commerce of the United States of America was filed with the Supreme Court of New Jersey, at the Hughes Justice Complex, 25 West Market Street, Trenton, New Jersey 08625-0970, via hand delivery.

I further certify that on the same date, a true and correct copy of the foregoing was served by overnight mail, postage prepaid, upon the following individuals:

Donna Siegel Moffa
Trujillo, Rodriguez & Richards
8 Kings Highway West
Haddonfield, NJ 08033

Marc Cuker
Williams, Cuker & Berzofsky
210 Lake Shore Drive East Suite 101
Cherry Hill, NJ 08002-1163

Michael J. Quirk
1717 Massachusetts Avenue, NW, Suite 800
Washington, DC 20036
Counsel for Appellant Jaliyah Muhammad

Marc Zucker
Susan Verbonitz
Weir & Partners LLP
20 Kings Highway West
Haddonfield, NJ 08033
Counsel for Respondent County Bank of Rehoboth Beach, Del.

J. Michael Kunsch
Sweeny & Sheehan, PC
Sentry Office Plaza
Suite 500, 216 Haddon Avenue
Westmont, NJ 08108

Claudia T. Callaway
Paul, Hastings, Janofsky & Walker LLP
875 15th Street, NW
Washington, DC 20005
Counsel for Respondent Main Street Service Corp.

William J. Pinilis
Pinilis Halpern, LLP
237 South Street, Lower Level
Morristown, NJ 07960

Deborah M. Zuckerman, AARP Foundation
Michael Schuster, AARP
601 E Street, NW
Washington, DC 20049
Counsel for Amici Curiae AARP, Consumers League of New Jersey and National Association of Consumer Advocates

Melville D. Miller, Jr.
David McMillin
Christopher Hill
Legal Services of New Jersey
100 Metroplex Drive
Suite 402
Edison, NJ 08818-1357
Counsel for Amicus Curiae Legal Services of New Jersey

Hon. Peter C. Harvey, Attorney General
Jeffrey Burstein
Carol Jacobson
Office of the Attorney General of New Jersey
R.J. Hughes Justice Complex
25 Market Street
Trenton, NJ 08625
Counsel for Amicus Curiae Attorney General of New Jersey

I hereby certify that the foregoing statements made by me are true. I am aware that if any of the foregoing statements made by me are willfully false, I am subject to punishment.

/s/
Andrew C. White

DATED: January 17, 2006

LOAN APPLICATION

County Bank of Rehoboth Beach, Delaware

Easy Cash 800-710-3400

YOU MAY BE APPROVED FOR UP TO $500 IF YOU MEET THESE SIMPLE REQUIREMENTS

- You must have been employed for at least 2 months if you have direct deposit and at least 4 months if you do not have direct deposit or you must be able to show other recurring income payments over the same time period.
- You must have a checking account with your name printed on the checks.
- You must be able to be contacted after work.
- You must have access to a fax machine.
- You must be at least 18 years old.
- You must have a gross income of at least $1500 per month, or a minimum of $1200 per month in Social Security or other benefits income.
- You must not be delinquent on a prior Loan from County Bank.

COMPLETE ALL THE FOLLOWING INFORMATION

Then FAX pages 1 and 2 of this APPLICATION, your BLANK VOIDED PERSONAL CHECK, your MOST RECENT PAYSTUB SHOWING YEAR TO DATE INCOME and your LAST PAYSTUB FROM 2002 OR W-2 to 610-667-3238.

PLEASE PRINT ALL INFORMATION NEATLY AND LEGIBLY USING BLACK INK

Current Personal Information			
Name: Jaliyah Muhammad		Phone:	
Address: 764 Scotland Rd Unit 42			
City: South Orange NJ		State: NJ	Zip: 07079
How long have you lived at this address? 1st 9 mos		Rent (X) Own ( )	
Social Security Number:		Birth Date:	
Phone number where we can send you a Fax?			
How did you hear about us? Friend			

Current Work and Bank Information			
Employer: (		Phone:	
Address:		Your Extension:	
City:		State:	Zip:
How long have you worked here? 1st 9 months		Hire Date:	
What is your position? Process S Research Rep I		Shift/Hours:	
What is your supervisor's name?		Superv. Phone:	
How much is your salary each pay period? * $			
How often are you paid? Weekly [X] Bi-weekly [ ] Twice Monthly [ ] Monthly [ ]			
What are your next two pay dates?	Next Pay Date:	Second Pay Date:	
Do you have a checking account? [X] Yes [ ] No			
Is your paycheck deposited directly into your checking account? * [X] Yes [ ] No			
E-mail address:			

* Or other source of income received periodically. Alimony, child support or separate maintenance income need not be revealed if you do not wish to have it considered as a source for repaying this obligation.

4 Personal Contacts – At Least 2 Must Be Relatives Not Living With You!			
	Name	Phone Number	Relationship
1			Mother
2			Sister
3			Sister
4			Sister

#22923

React

11/11/02 Page 1 of 3

APR 28 '03 09:28 PAGE.03

BEST AVAILABLE COPY

AGREEMENT TO ARBITRATE ALL DISPUTES: By signing below and to induce us, County Bank of Rehoboth Beach, Delaware, to process your application for a loan, you and we agree that any and all claims, disputes or controversies that we or our servicers or agents have against you or that you have against us, our servicers, agents, directors, officers and employees, that arise out of your application for a loan, the Loan Note or Agreement that you must sign to obtain the loan, this agreement to arbitrate all disputes, collection of the loan, or alleging fraud or misrepresentation, whether under the common law or pursuant to federal or state statute or regulation, including the matters subject to arbitration, or otherwise, shall be resolved by binding individual (and not class) arbitration by and under the Code of Procedure of the National Arbitration Forum ("NAF") in effect at the time the claim is filed. This agreement to arbitrate all disputes shall apply no matter by whom or against whom the claim is filed. Rules and forms of the NAF may be obtained and all claims shall be filed at any NAF office, on the World Wide Web at www.arb-forum.com, or at "National Arbitration Forum, P.O. Box 50191, Minneapolis, Minnesota 55405." *If you are unable to pay the costs of arbitration, your arbitration fees may be waived by the NAF.* The costs of any participatory, documentary or telephonic hearing, if one is held at your or our request, will be paid for solely by us as provided in the NAF Rules and. If a participatory hearing is requested, it will take place at a location near your residence. This arbitration agreement is made pursuant to a transaction involving interstate commerce. It shall be governed by the Federal Arbitration Act, 9 U.S.C. Sections 1-16. Judgment upon the award may be entered by any party in any court having jurisdiction. This Agreement To Arbitrate All Disputes is an independent agreement and shall survive the closing and repayment of the loan for which you are applying.

NOTICE: YOU AND WE WOULD HAVE HAD A RIGHT OR OPPORTUNITY TO LITIGATE DISPUTES THROUGH A COURT AND HAVE A JUDGE OR JURY DECIDE THE DISPUTES BUT HAVE AGREED INSTEAD TO RESOLVE DISPUTES THROUGH BINDING ARBITRATION.

AGREEMENT NOT TO BRING, JOIN OR PARTICIPATE IN CLASS ACTIONS: To the extent permitted by law, by signing below you agree that you will not bring, join or participate in any class action as to any claim, dispute or controversy you may have against us or our agents, servicers, directors, officers and employees. You agree to the entry of injunctive relief to stop such a lawsuit or to remove you as a participant in the suit. You agree to pay the costs we incur, including our court costs and attorney's fees, in seeking such relief. This agreement is not a waiver of any of your rights and remedies to pursue a claim individually and not as a class action in binding arbitration as provided above. This agreement not to bring or participate in class action suits is an independent agreement and shall survive the closing and repayment of the loan for which you are applying.

President, County Bank

(Borrower's Signature to the above Agreements Appears Below)

By signing this Application you certify that all of the information provided above is true, complete and correct and provided to us, County Bank of Rehoboth Beach, Delaware, for the purpose of inducing us to make the loan for which you are applying. By signing below you also agree to the Agreement to Arbitrate All Disputes and the Agreement Not To Bring, Join Or Participate In Class Actions and acknowledge receiving and reading the Application Supplement on page 3. We have retained Main Street Services Corp. (the "Company") to assist in processing your Application and to service your loan. By signing below you authorize us and the Company to share information in your Application and with regard to the processing, funding, servicing, repayment and collection of your loan. This Application will be deemed incomplete and will not be processed by us unless signed by you below.

Jalaluddin Mohammad 4-28-03 Jalaluddin S Mohammad

Print Name of Applicant Date Signature

CALL COUNTY BANK OF REHOBOTH BEACH, DELAWARE, AT (800) 710-3408, WITH ANY QUESTIONS REGARDING YOUR APPLICATION.

TELEFAX PAGES 1 AND 2, WHEN COMPLETED AND SIGNED, TO 610-667-3138.

LOAN NOTE AND DISCLOSURE

County Bank Of Rehoboth Beach, Delaware

Borrower's Name: JALIYAH MUHAMMAD Loan # 3-00574530 Date: April 27, 2003

Parties: In this Loan Note and Disclosure ("Note") you are the person named as Borrower above. We are the lender, County Bank of Rehoboth Beach, Delaware

The Account: You have deposit account, No ____ ____ ("Account"), with us or, if the following space is completed, at _____ ("Bank"). You authorize us to effect a credit entry to deposit the proceeds of the Loan (the Amount Financed indicated below) to your Account at the Bank.

DISCLOSURE OF CREDIT TERMS: The information in the following disclosure box is part of this Note:

ANNUAL PERCENTAGE RATE	FINANCE CHARGE	Amount Financed	Total of Payments
The cost of your credit as a yearly rate. (e) 646.1 %	The dollar amount the credit will cost you. $ 30.00	The amount of credit provided to you or on your behalf. $ 100.00	The amount you will have paid after you have made the scheduled payment. $ 130.00

Your Payment Schedule will be: 1 payment of $ 130.00 due on 05/16/2003

Security: This loan is unsecured.

Prepayment: If you prepay your loan in advance, you will not receive a refund of any Finance Charge.

(e) The Annual Percentage Rate is an estimate based on the anticipated date the proceeds will be deposited to or paid on your account, which is 04/29/2003

See below and your other contract documents for any additional information about prepayment, nonpayment and default.

ITEMIZATION OF AMOUNT FINANCED of $ 100.00 ; given to you directly: $ 100.00 ; paid on your account: $ 0.00

PROMISE TO PAY: You promise to pay to us or to our order, in 1 payment, on the date indicated in the Payment Schedule, the Total of Payments. On or after the day your Loan comes due you authorize us to effect one or more ACH debit entries to your Account at the Bank. You may revoke this authorization at any time up to 3 business days prior to the due date. However, if you timely revoke this authorization, you authorize us to prepare and submit one or more checks drawn on your Account to repay your loan when it comes due. If your Account is with us, you authorize us to deduct the payment from your Account on the day the loan comes due. If there are insufficient funds on deposit in your Account to effect an ACH debit entry or to pay a check or otherwise cover the loan payment on the due date, you promise to pay us all sums you owe by mailing a check or Money Order payable to "County Bank", c/o Easy Cash P.O. Box 915, Bala Cynwyd, PA 19004.

PREPAYMENT: If a Finance Charge remains after a Loan Due date is earned in full at the time the Loan is funded. You may pay all or part of what you owe prior to the due date, without penalty. However, if you pay early you will not be entitled to a refund of part or all of the Finance Charge.

EXCHANGE OF CREDIT INFORMATION: We have retained Main Street Services Corp. (the "Company") to service your loan. You authorize us and the Company to share information in connection with the application, processing, funding, servicing, repayment and collection of your loan.

NOTICE: YOU MUST CALL US, AT (800) 710-3400, BETWEEN 9:00 A.M. AND 10:00 A.M., 3 BUSINESS DAYS PRIOR TO THE DUE DATE TO FACILITATE THE PAYMENT OF YOUR LOAN.

RETURN ITEM FEE: You agree to pay $30 if an item in payment of what you owe is returned unpaid or an ACH debit entry, the authorization for which was not properly revoked by you, is rejected by the Bank for any reason.

GOVERNING LAW: This Note is governed by Delaware law, except as federal laws may apply.

AGREEMENT TO ARBITRATE ALL DISPUTES: You and we agree that any and all claims, disputes or controversies between you and us and/or the Company, any claim by either of us against the other or the Company (or the employees, officers, directors, agents or assigns of the other or the Company) and any claim arising from or relating to your application for this loan or any other loan you previously, now or may later obtain from us, this Loan Note, this agreement to arbitrate all disputes, your agreement not to bring, join or participate in class actions, regarding collection of the loan, alleging fraud or misrepresentation, whether under the common law or pursuant to federal, state or local statute, regulation or ordinance, including disputes as to the matters subject to arbitration, or otherwise, shall be resolved by binding individual (and not joint) arbitration by and under the Code of Procedure of the National Arbitration Forum ("NAF") in effect at the time the claim is filed. This agreement to arbitrate all disputes shall apply no matter by whom or against whom the claim is filed. Rules and forms of the NAF may be obtained and all claims shall be filed at any NAF office, on the World Wide Web at www.arb-forum.com, by telephone at 800-474-1371, or at "National Arbitration Forum, P.O. Box 50191, Minneapolis, Minnesota 55405." Your arbitration fee may be waived by the NAF in the event you cannot afford to pay them. The cost of any participatory, documentary or telephone hearing, if one is held at your or our request, will be paid for solely by us as provided in the NAF Rules and, if a participatory hearing is requested, it will take place at a location near your residence. This arbitration agreement is made pursuant to a transaction involving interstate commerce. It shall be governed by the Federal Arbitration Act, 9 U.S.C. Sections 1-16. Judgment upon the award may be entered by any party in any court having jurisdiction.

NOTICE: YOU AND WE WOULD HAVE HAD A RIGHT OR OPPORTUNITY TO LITIGATE DISPUTES THROUGH A COURT AND HAVE A JUDGE OR JURY DECIDE THE DISPUTES BUT HAVE AGREED INSTEAD TO RESOLVE DISPUTES THROUGH BINDING ARBITRATION.

AGREEMENT NOT TO BRING, JOIN OR PARTICIPATE IN CLASS ACTIONS: To the extent permitted by law, you agree that you will not bring, join or participate in any class action as to any claim, dispute or controversy you may have against us, our employees, officers, directors, servicers and assigns. You agree to the entry of injunctive relief to stop such a lawsuit or to remove you as a participant in the suit. You agree to pay the attorney's fees and court costs we incur in seeking such relief. This Agreement does not constitute a waiver of any of your rights and remedies to pursue a claim individually and not as a class action in binding arbitration as provided above.

SURVIVAL: The provisions of this Note dealing with the Agreement to Arbitrate All Disputes and the Agreement Not To Bring, Join Or Participate in Class Actions shall survive repayment in full and/or default of this Note.

BANKRUPTCY: You represent that you have not recently filed nor do you currently intend to file for bankruptcy.

BY SIGNING BELOW, YOU AGREE TO ALL OF THE TERMS OF THIS NOTE, INCLUDING THE AGREEMENT TO ARBITRATE ALL DISPUTES AND THE AGREEMENT NOT TO BRING, JOIN OR PARTICIPATE IN CLASS ACTIONS. YOU ALSO ACKNOWLEDGE RECEIPT OF A FULLY COMPLETED COPY OF THIS NOTE.

INSTRUCTIONS: THIS NOTE IS SUBJECT TO BANK APPROVAL. Read the entire Note. If all of the loan terms are acceptable to you, date and sign at right and fax this Note to (610) 667-3138. If approved, the loan proceeds will be deposited to your Account indicated above.

x _____ 4-28-03

Borrower's Signature Date

167 589 777 22923

STL-1 04/04/02 EC

© 2002 County Bank

JALIYAH MUHAMMAD (7)

PASSED 10C

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No. 06-907

Supreme Court, U.S.
FILED
MAR 6 - 2007
OFFICE OF THE CLERK

In The Supreme Court of the United States

COUNTY BANK OF REHOBOTH BEACH, DELAWARE AND MAIN STREET SERVICE CORPORATION,

Petitioners,

v.

JALIYAH MUHAMMAD, ON BEHALF OF HERSELF AND ALL OTHERS SIMILARLY SITUATED,

Respondent.

On Petition For A Writ Of Certiorari To The Supreme Court Of New Jersey

RESPONDENT'S BRIEF IN OPPOSITION

F. PAUL BLAND, JR.
Counsel of Record
PUBLIC JUSTICE, P.C.
1825 K Street, Suite 200
Washington, DC 20006
(202) 797-8600

DONNA SIEGEL MOFFA
TRUJILLO, RODRIGUEZ & RICHARDS
8 Kings Highway West
Haddonfield, NJ 08033
(856) 795-9002

MICHAEL J. QUIRK
MARK R. CUKER
WILLIAMS CUKER BEREZOFSKY
210 Lake Drive East, Suite 101
Cherry Hill, NJ 08002
(856) 667-0500

Counsel for Respondent

COCKLE LAW BRIEF PRINTING CO. (800) 225-6964
OR CALL COLLECT (402) 342-2831

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INTRODUCTION

The decision below favors arbitration by prohibiting exculpatory contract terms that prevent arbitration from ever occurring. This Petition arises from a state court order *compelling the parties to arbitrate*. What Petitioners are now seeking is not the right to arbitrate, which they already have, but a right to compel arbitration under rules that unduly favor them by preventing Respondents from vindicating their state-law claims. No one disputes that federal law gives Petitioners and other companies a general right to enforce contracts for arbitration. But this is not an unlimited right that forces courts to rubber-stamp any arbitration terms a company can devise. Instead, the Federal Arbitration Act ("FAA") makes arbitration clauses revocable "upon such grounds as exist at law or in equity for the revocation of any contract." 9 U.S.C. § 2.

Because the plaintiffs' claims here are quite complex, but small in value, the New Jersey Supreme Court held that the Petitioners' contract term banning class actions was effectively an illegal exculpatory clause. Because a longstanding body of generally applicable New Jersey contract law arising in settings that have nothing to do with arbitration holds that exculpatory contract terms are unenforceable, the New Jersey Supreme Court struck that term as unenforceable before ordering the parties to arbitrate. The issue here thus is not whether arbitration is *ever* allowed, but whether federal law overrides generally applicable New Jersey contract law prohibiting exculpatory terms in contracts of adhesion merely because those terms are embedded in an arbitration clause. For each of the following reasons, the New Jersey Supreme Court's resolution of this question does not warrant review.

As a preliminary matter, the Petition should be rejected because this Court does not have jurisdiction. The ruling below compelling the parties to arbitrate is not a final judgment under 28 U.S.C. § 1257(a), and this case does not fall within any of the four exceptions to the final judgment rule recognized in *Cox Broadcasting Corp. v. Cohn*, 420 U.S. 469 (1975).

Even if the Court did have jurisdiction, it still should not grant the Petition. The Petition raises three issues. The first issue poses a theory of federal law that has never been adopted by any state high court or federal appellate court. The second and third issues posed in the Petition were not timely raised in the state courts below, present no split of authority, and also are wholly lacking in merit. For all of these reasons, the Petition should be denied.

STATEMENT OF THE CASE

A. The Underlying Transactions And State Law Claims

Plaintiff Jaliyah Muhammad was a part-time student at a business school when she took out her first payday loan to pay for her school books. On May 26, 2003, Ms. Muhammad obtained a $200 payday loan from the defendants in exchange for a loan note requiring a lump sum payment of $260 (including a $60 finance charge) by June 13. This amounts to an interest rate of 608.33%. When she could not repay this balance, she twice paid additional $60 charges to extend the same $200 principal. In total, she paid $180 interest on a $200 loan she had for under two months.

Although Ms. Muhammad's loan papers listed County Bank as the lender, Ms. Muhammad alleges that the actual lender was Easy Cash, which marketed these loans to New Jersey consumers through the mass media and over the Internet. After the consumer signs a loan form and transmits it to Easy Cash by telephone, fax, or over the Internet, Easy Cash arranges to transfer funds to the consumer's checking account.

Ms. Muhammad filed a putative class action in State court claiming that these loans violated New Jersey's civil usury limit of 16% APR (NJSA § 31:1-1(a)), as well as its criminal usury limit of 30% APR (NJSA § 2C:21-19). She alleged that Easy Cash conspired to evade New Jersey's usury laws by naming County Bank as the lender when, *in fact*, it was the Easy Cash defendants who financed, marketed, originated, and serviced these loans, and bore all of the risk through an agreement to indemnify County Bank. This sort of arrangement is often referred to as a "rent a bank" scheme, and has been sharply criticized by federal regulators (among others). *See*, *e.g.*, Office of Comptroller of Currency News Release 2003-06 (Jan. 31, 2003) ("We have been greatly concerned with arrangements in which national banks essentially rent out their charter to third parties who want to evade state and local consumer protection laws.") Plaintiff claimed that this enterprise violated New Jersey's Consumer Fraud Act ("CFA") and its RICO statute's prohibition against criminal usury racketeering. Ms. Muhammad also charged that County Bank's involvement in this enterprise violated the CFA's and State RICO statute's separate prohibitions against aiding and abetting usury.

Petitioners responded to Ms. Muhammad's lawsuit first by removing the case to federal court based on a

"complete preemption" argument. Pet. A17. After this argument failed and the case was remanded, Petitioners next moved the State court to bar Ms. Muhammad's class claims and compel her to arbitrate an individual action. In support of this motion, Petitioners invoked a mandatory arbitration clause in their payday loan contracts. The primary operative sentence of Petitioners' arbitration clause is 157 words long. In addition to requiring arbitration, this clause barred Petitioners' customers from bringing or participating in class actions. The clause also incorporated the rules of procedure of the National Arbitration Forum ("NAF"). One of those rules limited the discovery available to parties to an amount commensurate with the value of their claims. Under this rule, if Ms. Muhammad were required to proceed on an individual basis, she would only be permitted to take discovery commensurate with her $180 damages claim in support of her allegation that the whole rent-a-bank structure was a sham to conceal who the true lender was.[1] The NAF's rules also included a "loser pays" term, which permits arbitrators to force any consumer who does not prevail on her claims to pay the defendant's attorney fees and arbitration costs.

Ms. Muhammad opposed Petitioners' motion on the grounds that the arbitration clause is unconscionable under New Jersey law in light of its adhesive and exculpatory terms. Under established New Jersey law, a

[1] Proving this allegation is essential to hers and the class members' claims because, absent such proof, a finding that County Bank is the lender defeats her claims under a federal preemption doctrine that allows a Delaware bank to make loans in New Jersey while ignoring its laws governing interest rates.

non-negotiable adhesive contract provision is unconscionable if there is a disparity in sophistication and bargaining power between the parties *and* the provision's terms are either exculpatory or unreasonably one-sided in favor of the drafter. *See Rudbart v. North Jersey District Water Supply Comm'n*, 605 A.2d 681 (N.J. 1992). With respect to the first prongs of this argument, the record contained copies of the arbitration clauses of all of the defendants' competitors, establishing that clauses banning class actions and using NAF are pervasive in the payday lending industry. The record also established that Petitioners' mandatory arbitration clause is a non-negotiable, adhesive provision imposed by experienced lending companies against payday loan borrowers with limited commercial experience and credit options. The arbitration clause is a pre-printed, standard form provision, transmitted between borrower and lender by facsimile with no opportunity for negotiation. With respect to the exculpatory and one-sided effect of the arbitration clause's terms, the record established that since County Bank began putting its name on payday loans nationwide in 1997, only two (2) customers have ever even attempted to arbitrate claims.

The State trial court rejected Ms. Muhammad's argument and held that the arbitration clause's terms prohibiting her class claims were enforceable. The New Jersey Superior Court, Appellate Division, affirmed.

B. The New Jersey Supreme Court's Decision

After granting Ms. Muhammad's petition for leave to file an interlocutory appeal, the New Jersey Supreme Court reversed in part by holding that the class arbitration ban was unconscionable, but severable, so that the

arbitration clause could still be enforced. The court began its discussion with a recognition of the federal policy favoring arbitration, Pet. A19, while noting this Court's decisions directing that the FAA does not preclude an examination into whether a given arbitration clause is unconscionable under state law. *Id.*

The New Jersey Supreme Court then addressed New Jersey's standard for finding unconscionability, a "multi-factor analysis" that had been developed in a series of cases none of which involved the enforcement of arbitration clauses. In particular, the court relied heavily upon the considerations set forth in its prior decision in *Rudbart*, *supra*. *E.g.,* Pet. A12, A22, A23, A25-A26. The court then noted the pivotal and longstanding rule that, "[i]n New Jersey, exculpatory waivers that seek a release from a statutorily imposed duty are void as against public policy. *McCarthy v. NASCAR, Inc.*, 226 A.2d 713 (1967)." Pet. A27. The court discussed prior New Jersey law, as well as decisions from this Court and numerous other courts, establishing that, in certain circumstances (particularly those involving small-value claims), the class action device offers the only means for individuals to effectively vindicate their rights. Pet. A26-A29. The court distinguished, but did not overrule, a prior decision by an intermediate appellate court in New Jersey, *Gras v. Associates First Capital Co.*, 786 A.2d 886 (N.J. App. Div. 2001). Pet. A29.

The court explained that its decision was consistent with New Jersey's policy favoring arbitration, because "[n]othing in the arbitration process requires that claims be brought only by individuals." Pet. A30. The court also noted the consistency between its decision and this Court's

statement that "arbitration is allowed in actions authorized by federal statutes '[s]o long as the prospective litigant effectively may vindicate [his or her] statutory cause of action in the arbitral forum.'" Pet. A31, citing *Gilmer v. Interstate/Johnson Lane Corp.*, 500 U.S. 20, 28 (1991). The Court pointedly added, twice, that it would have reached the same conclusion on unconscionability of the class action ban had it appeared with *or without* an arbitration clause. Pet. A12, A29.

The court then held that the provision banning class actions was severable from the remainder of the arbitration agreement, Pet. A33-A34, and thus ordered the parties to proceed to arbitration with that provision stricken. Pet. A34.

REASONS FOR DENYING THE PETITION

I. The Court Lacks Jurisdiction Over This Interlocutory State Court Order Compelling Arbitration.

A. The Decision Below Is Not a Final Judgment Under 28 U.S.C. § 1257(a).

This Court has jurisdiction to review "[f]inal judgments or decrees rendered by the highest court of a State in which a decision could be had . . . " 28 U.S.C. § 1257(a). Section 1257(a) establishes a "firm final judgment rule." *Jefferson v. City of Tarrant, Ala.*, 522 U.S. 75, 81 (1997). This means that a state court's decision must be "final as an effective determination of the litigation and not merely of interlocutory or intermediate steps therein." *Id.* Section 1257's requirement of finality " 'is not one of those technicalities to be easily scorned. It is an important factor in

the smooth working of our federal system.'" *Id.* (quoting *Radio Station WOW, Inc. v. Johnson*, 326 U.S. 120, 124 (1945)). Here, since the New Jersey Supreme Court did not issue a final judgment or decree, this Court lacks jurisdiction under § 1257(a).

After finding County Bank's class-action ban unenforceable, the New Jersey Supreme Court held that the waivers were severable so that "the remainder of the arbitration agreement is enforceable." Pet. A33. In remanding the case to the state trial court "for proceedings consistent with this opinion" (Pet. A34), the New Jersey Supreme Court ordered the parties to arbitrate Ms. Muhammad's claims. This order thus is not final as an "effective determination of the litigation." *Jefferson*, 522 U.S. at 81.

Indeed, orders compelling arbitration without dismissing claims are not final or appealable as of right under either federal or New Jersey law. *See* 9 U.S.C. § 16(b) (except under the permissive appeal provisions of 28 U.S.C. § 1292(b), appeal may not be taken from an "interlocutory" order directing arbitration or staying litigation in favor of arbitration); *Wein v. Morris*, 909 A.2d 1186, 1194 (N.J. Super. App. Div. 2006) ("A stay of an action pending arbitration does not constitute a final, appealable order because it inherently anticipates further proceedings prior to the ultimate entry of a final judgment."); *see also id.* n.6 (noting that subsequently enacted N.J. Uniform Arbitration Act "does not appear to expressly permit an appeal from an order staying an action and compelling arbitration.").[2] The decision below compelling arbitration thus is not a final judgment under § 1257(a).

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[2] In the proceedings below, Ms. Muhammad did not have an appeal of right to the New Jersey Supreme Court. Instead, she had to obtain

(Continued on following page)

B. The *Cox Broadcasting* Exceptions to § 1257's Final Judgment Rule Do Not Apply.

Under *Cox Broadcasting Corp. v. Cohn*, 420 U.S. 469 (1975), the Court may review state court decisions prior to a final judgment in four narrow circumstances. The first involves cases where "there are further proceedings . . . yet to occur in the state courts but where for one reason or another the federal issue is conclusive or the outcome of further proceedings preordained." *Id.* at 479. Second are cases in which "the federal issue, finally decided by the highest court in the State, will survive and require decision regardless of the outcome of future state-court proceedings." *Id.* at 480. Third are cases where "the federal claim has been finally decided with further proceedings on the merits in the state courts to come, but in which later review of the federal issue cannot be had, whatever the ultimate outcome of the case." *Id.* at 481. The fourth exception arises where (a) "the federal issue has been finally decided in the state courts . . . and where reversal of the state court on the federal issue would be preclusive of any further litigation on the relevant cause of action"; *and* (b) "a refusal immediately to review the state-court decision might seriously erode federal policy." *Id.* at 482-83. None of these exceptions to § 1257(a)'s final-judgment rule applies here.

The first three *Cox Broadcasting* exceptions do not apply because all claims and defenses on the merits are yet to be resolved, and thus could be subject to later appeals. This is not a case where "the federal issue is

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leave for an interlocutory appeal. *See* Pet. A18, B19. New Jersey law does not have an equivalent to 28 U.S.C. § 1257(a) requiring a final judgment for all appeals.

conclusive" in further proceedings or the outcome of these proceedings is "preordained," 420 U.S. at 479, because either party could still prevail on its unresolved merits claims or defenses. The first exception thus does not apply. Nor does the second exception apply because, if Muhammad fails to prove her state-law claims or County Bank prevails on a merits defense, the federal question asserted here would not "survive and require decision." *Id.* at 480. Likewise, the third exception does not apply because there is no state-law bar to a later appeal by any party, *id.* at 481, in the event of an adverse judgment. To the contrary, New Jersey law expressly recognizes a party's right to an appeal after arbitration proceedings are completed. *See* NJSA § 2A:23B-28(a)(3) ("An appeal may be taken from an order confirming or denying confirmation of an [arbitral] award.").

Finally, the fourth *Cox Broadcasting* exception likewise does not apply here for two independent reasons. First, a reversal of the decision below on the federal issue asserted would not as a matter of law "be preclusive of any further litigation on the relevant cause of action," 420 U.S. at 482-83, since Ms. Muhammad would retain her individual state-law claims, whether or not she could effectively vindicate them. Thus, the Petition fails to meet the fourth exception. Moreover, this is not a case where "a refusal to review the state-court decision might seriously erode federal policy." *Id.* at 483. The Court has applied this exception to allow interlocutory appeals from state court orders *denying* arbitration, finding that "to delay review of a state judicial decision denying enforcement of the contract to arbitrate until the state-court litigation has run its course would defeat the core purpose of a contract to arbitrate." *Southland Corp. v. Keating*, 465 U.S. 1, 7-8

(1984). The decision below, however, *compelled* arbitration of Ms. Muhammad's claims. Thus, a refusal to grant immediate review here that allows the parties to arbitrate would not erode federal policy favoring arbitration. For each of these reasons, the New Jersey Supreme Court's decision does not fall within *Cox Broadcasting*'s fourth exception.

In sum, this case presents no basis to depart from § 1257(a)'s imposition of a "firm final judgment rule." The Court thus lacks jurisdiction, and the petition should be denied.

II. The Federal Arbitration Act Preemption Issue Raised in the Petition Does Not Merit Review.

A. There Is No Split of Authority on Petitioners' FAA Preemption Argument.

As set forth above, in this case, the New Jersey Supreme Court held that Petitioners' contract provision banning class actions was unconscionable, because under the facts of this case (involving very complicated and difficult-to-prove, but individually small claims), it would serve as an exculpatory clause and exculpatory clauses embedded in contracts of adhesion are unconscionable under New Jersey contract law. The Petition argues that even if a contractual provision banning consumers from bringing or participating in a class action is unconscionable under normal state doctrines of contract law, this body of state law is nonetheless preempted by the FAA. *E.g.*, Pet. 19. The Court below rejected Petitioners' argument that the FAA preempts normal state principles of contract law. To establish a conflict between the decision of the New Jersey Supreme Court and other state high

courts or federal appellate courts, Petitioners must identify *some* such court holding that even though a contract term banning class actions embedded in an arbitration clause is unconscionable under state law, that rule of state law is nonetheless preempted by the FAA. Petitioners do not cite to any such case, and there is none.[3] There are courts that have enforced class action bans in given cases, but each was decided on grounds unrelated to the federal legal theory advanced in the petition. In sum, Petitioners never identify a split of appellate authority on the federal law question raised in the Petition.[4]

Instead, Petitioners point to inapposite cases to generate the appearance of a conflict. For example, the Petition alleges a conflict between the lower court here and a number of cases where courts have held that the language and legislative history of certain other federal statutes do not conflict with the FAA. *E.g.*, Pet. at 4, 17 (citing *Johnson v. W. Suburban Bank*, 225 F.3d 366 (3d Cir. 2000)). The Petition claims that the decision below represents a split with *Johnson* that would result in the

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[3] The closest Petitioners come (Pet. 14-16) is a case from a Tennessee intermediate appellate court, *Pyburn v. Bill Heard Chevrolet*, 63 S.W.3d 351, 365 (Tenn. Ct. App. 2001), and a case from a federal trial court in West Virginia. *Schultz v. AT&T Wireless Servs., Inc.*, 376 F. Supp.2d 685, 691 (N.D. W. Va. 2005)). *Pyburn* does not represent the view of a state court of last resort, *see* S. Ct. Rule 10, and in any event held that a class action ban at issue was not unconscionable *under state law*. Accordingly, *Pyburn*'s preemption discussion was unnecessary to its holding and thus is pure dicta.

[4] The Petition blurs this fact through the use of vague language. It states, for example, that "[t]he question divides" state and federal courts, Pet. at 12, but does not say *which* question divides those courts. As will be shown, none of the cases cited support the proposition that the question of federal law advanced in the opinion divides those courts.

law being different in federal courts in New Jersey and in New Jersey state courts. Pet. at 17. But *Johnson* does not conflict with the opinion below because it did not hold that state law relating to a class action ban was preempted by the FAA. Instead, *Johnson*'s holding allowing enforcement of an arbitration clause's class-action prohibition turns upon the language and legislative history of the federal Truth in Lending Act ("TILA").[5] This case says nothing about the FAA's relationship to state contract law.[6]

In fact, the Third Circuit – in sharp contrast to Petitioners' approach – holds that the question of the unconscionability of an arbitration clause term banning class claims is one of state, not federal, law. Petitioners repeatedly cite to the New Jersey Supreme Court's decision in *Delta Funding Corp. v. Harris*, 912 A.2d 104 (N.J. 2006) for its policy arguments, but that case was certified to the state court *by the Third Circuit*, *id.* at 108, for a determination of whether provisions in a mandatory consumer arbitration clause, including its class action waiver, *id.* at 115, were unconscionable under New Jersey law. The Third Circuit's certification and subsequent embrace of the

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[5] The proper interpretation of TILA was also the issue in *Randolph v. Green Tree*, 244 F.3d 814 (11th Cir. 2001), Pet. at 4, and thus that case also does not pose a conflict on the federal law issue presented in this Petition.

[6] That *Johnson*'s holding is based on unique considerations relating to TILA claims is demonstrated by the Third Circuit's subsequent finding in a case involving claims under the Fair Debt Collection Practices Act ("FDCPA") that class actions appear to be fundamental to the statutory structure of the FDCPA, so that "lacking this procedural mechanism meritorious FDCPA claims might go unaddressed because *the awards in an individual case might be too small to prosecute an individual action.*" *Weiss v. Regal Collections*, 385 F.3d 337, 345 (3d Cir. 2004) (emphasis added).

New Jersey Supreme Court's opinion applying state contract law, *see Delta Funding Corp. v. Harris*, 466 F.3d 273 (3d Cir. 2006), demonstrate that the Third Circuit squarely rejects the federal preemption theory Petitioners espouse here.

Likewise, Petitioners cannot manufacture a split by pointing to cases where the general contract laws of states other than New Jersey do not consider class action bans to be exculpatory. *See* Pet. at 15 (acknowledging that various state court holdings enforcing class action bans are based upon state unconscionability law). This Court does not sit to resolve differences among the states relating to their contract law doctrines governing exculpatory clauses. This is particularly so under the FAA, whose savings clause calling for the application of state contract law principles to arbitration clauses makes the existence of such differences in result inevitable.

In one example of this confusion of state and federal law, the Petition mis-cites *Iberia Credit Bureau, Inc. v. Cingular Wireless LLC*, 379 F.3d 159 (5th Cir. 2004), to allege the existence of a split justifying this Court's review of the FAA question presented here. Pet. at 16. In fact, the difference between the holding in *Iberia* and the holding of the New Jersey Supreme Court this case is based entirely on a difference in state law. The two cases are entirely consistent on the *federal* law issue raised in the Petition. The reason the Fifth Circuit upheld the class action ban at issue in *Iberia* was because there is no general Louisiana policy in favor of class actions in consumer litigation. In making its unconscionability determination, the court noted that the Louisiana Unfair Trade Practices Act (LUTPA) does not permit class actions, and that Louisiana law recognizes alternative remedies to class actions. 379

F.3d at 174-75 (citing La. Rev. Stat. Ann. § 51:1409(A)). *Iberia* acknowledged that the enforceability of a class action ban is a question of state law, distinguishing (rather than disagreeing with) a Ninth Circuit case that held that an arbitration clause barring class actions was unconscionable under California law on the grounds of the difference in state law between California and Louisiana. 379 F.3d at 174 (citing *Ting v. AT&T*, 319 F.3d 1126, 1150 (9th Cir. 2003), *cert. denied*, 540 U.S. 811 (2003)).

The same is true of *Caley v. Gulstream Aerospace Corp.*, 428 F.3d 1359 (11th Cir. 2005) (cited at Pet. 16), where the court upheld a class action ban based upon its reading of Georgia state contract law. 428 F.3d at 1379. The court did not even mention preemption, and like *Iberia* distinguished (rather than disagreed with) a Ninth Circuit case applying the different contract law of California. *Id.* at 1378 (distinguishing *Ingle v. Circuit City Stores, Inc.*, 328 F.3d 1165 (9th Cir. 2003)).

Similarly, the Petition asserts a conflict with *Snowden v. CheckPoint Check Cashing*, 290 F.3d 631 (4th Cir. 2002). Pet. 4, 17. As with *Iberia*, *Caley*, and numerous other cases cited in the Petition, *Snowden* does not conflict with the decision below on any issue of federal law, however, but merely reflects that Maryland's state law of exculpatory clauses differs from the law in New Jersey. *See, e.g.*, *Walther v. Sovereign Bank*, 872 A.2d 735, 750 (Md. 2005).

In sum, these cases are only in conflict with the decision below in the sense that the contract laws of New Jersey, Louisiana, Maryland and Georgia differ. There is no split of authority on the federal law question presented. For this reason alone, the Petition should be denied.

B. The Decision Below Does Not Conflict With This Court's Decisions.

1. The Petition's Principal Argument Is Contrary to this Court's Decisions Applying the FAA.

The Petition repeatedly argues that arbitration agreements must always be enforced in their entirety, precisely as written, without any interference with state law. *E.g.*, Pet. at 19. This argument ignores the FAA's savings clause, and this Court's decisions interpreting it.

As the Court below established at some length, New Jersey law disfavoring adhesive exculpatory contracts is part of the State's general law of unconscionability and public policy governing *all* contracts. Under this Court's decisions applying the FAA, this general contract law applies to arbitration clauses just as it does to any other contract term. *See Doctor's Assoc's, Inc. v. Casarotto*, 517 U.S. 681, 687 (1996) ("[G]enerally applicable contract defenses such as fraud, duress or unconscionability, may be applied to invalidate arbitration agreements without contravening [9 U.S.C. § 2]."); *Gilmer v. Interstate Johnson Lane Corp.*, 500 U.S. 20, 33 (1991) ("courts should remain attuned to well-supported claims that the agreement resulted from the sort of fraud or overwhelming economic power that would provide grounds for the revocation of any contract.") (quoting *Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc.*, 473 U.S. 614, 627 (1985)) (internal quotation omitted).

2. This Court's Decision in *Bazzle* Demonstrates that the Decision Below Was Correct.

Petitioners argue that this Court's decision in *Green Tree Financial Corp. v. Bazzle*, 539 U.S. 444 (2003) should be read as holding that courts may not "vary" from contract terms with respect to bans on class actions if those terms are embedded in arbitration clauses. Pet. at 5 (citing to a dissent in *Bazzle*). In fact, nothing in *Bazzle* supports Petitioners' argument – *Bazzle* did not involve an unconscionability challenge to a class action ban and did not involve the FAA's savings clause.

In fact, *Bazzle* disproves one of Petitioners' central assumptions: that a contract term banning class actions is inherently part of any agreement to arbitrate. The Petition argues, for example, that if the decision below (which enforced the agreement to arbitrate but struck the class action ban) is enforced, that all businesses will have to fear that "their arbitration agreements" will all be invalidated. Pet. at 18. In Petitioners' world, class action bans are inseparable from arbitration clauses. *See also* Pet. at 4 (asserting that courts may never order class-wide arbitration unless parties have expressly agreed to that proceeding, the same theory as was unsuccessfully advanced in *Bazzle*).

This theory was rejected by six Justices of this Court in *Bazzle*. In *Bazzle*, the plurality held that, where an arbitration clause does not explicitly allow the arbitrator to proceed on a class basis, the question of whether the arbitration may proceed on that basis is "a matter of state law." 539 U.S. at 447. Two other Justices would have left undisturbed the decision of the South Carolina Supreme Court, which – contrary to Petitioners' proposed rule of

federal law – permitted class-wide arbitration. Although Petitioners continue to insist that class actions are inherently inconsistent with arbitration, courts throughout the United States applying *Bazzle* in the last several years have rejected similar arguments and instead have held that cases could proceed in arbitration on a class action basis in cases where the arbitration clauses did not expressly authorize class action treatment.[7]

As further proof that class actions are not inconsistent with arbitration, shortly after this Court issued its decision in *Bazzle*, the American Arbitration Association ("AAA") adopted a new set of rules for handling class actions in arbitration. *E.g.*, Carole J. Buckner, *Toward a Pure Arbitral Paradigm of Classwide Arbitration: Arbitral Power and Federal Preemption*, 82 Denv. U. L. Rev. 301 (2004) ("The AAA promulgated the first set of classwide arbitration rules in October 2003, following the *Bazzle* decision."). As of this writing, AAA lists over 100 cases being heard under its "Supplementary Rules for Class Arbitrations." *See* American Arbitration Association, "Class Arbitration Case Docket" (available at www.adr.org/Classarbitration policy). Under Petitioners' theory, the American Arbitration Association has been actively undercutting the FAA for the past three years since *Bazzle* was decided.

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[7] *See, e.g., Pedcor Mgmt. Co. v. Nat'l Personnel of Texas*, 343 F.3d 355 (5th Cir. 2003); *Genus Credit Management Corp. v. Jones*, 2006 WL 905936 (D. Md. April 6, 2006); *Veliz v. Cintas Corp.*, 2005 WL 1048699 at *5 (N.D. Cal. May 4, 2005); *Ramirez v. Cintas Corp.*, 2005 WL 659984 at *10-11 (N.D. Cal. Mar. 22, 2005); *In re Wood*, 140 S.W.3d 367 (Tex. 2004); *Bess v. DirecTV, Inc.*, 815 N.E.2d 455, 460 (Ill. App. 2004); and *Garcia v. DirecTV, Inc.*, 9 Cal. Rptr. 3d 190, 195-96 (Cal. App. 2004).

Accordingly, after *Bazzle*, there is no reason why a decision finding that a class action ban is unconscionable even implicates the FAA. A contract can include a class action ban without including an arbitration provision, or a contract could include an arbitration agreement without a class action ban. The FAA does not allow a party to evade state contract law "merely because the prohibiting or limiting provisions are part of or tied to provisions in the contract relating to arbitration." *State ex rel. Dunlap v. Berger*, 567 S.E.2d 265 (W. Va. 2002), *cert. denied*, 537 U.S. 1087 (2002). Nothing in the FAA permits parties to launder otherwise illegal contract terms and make them legal merely by placing them under the heading "arbitration."

3. The Decision Below Is Consistent With This Court's Decision in *Gilmer*.

Petitioners also argue that this Court held that arbitration clauses are enforceable even where they do not provide for class actions, citing to this Court's decision in *Gilmer*. Pet. at 5. This argument misreads *Gilmer*. First, unlike the arbitration clause at issue here, the clause in *Gilmer* allowed for class arbitrations. 500 U.S. at 32 (noting that collective relief could be obtained in arbitration). Therefore, unlike the plaintiffs here, the *Gilmer* plaintiff would not be deprived of a class remedy if arbitration were compelled on the terms set forth in the contract. Second, *Gilmer* was not a class action, but an individual civil rights action seeking damages substantially greater than the damages sought here. Thus, the availability of a class action was not necessary for the *Gilmer* plaintiff to obtain relief.

In addition, in *Gilmer*, the Court was interpreting the text and structure of the federal Age Discrimination in Employment Act, not a state law challenge to an arbitration clause such as those permitted under § 2 of the Federal Arbitration Act. The case contains no discussion of state law dealing with exculpatory clauses (or any other topic of state law). Moreover, in *Gilmer* there was no reason to imagine that a class action ban would prevent the plaintiff from effectively vindicating his substantive rights. Indeed, Congress was evidently aware that ADEA claims (typically claims that a person at the peak of her earning power was wrongfully terminated) are unlike small consumer claims, and that class actions are generally not necessary to provide a remedy to such plaintiffs. This is demonstrated in part by the fact that class actions under the ADEA proceed on an opt-in basis rather than the normal opt-out process such as that under Rule 23(b)(3). *See, e.g., Allen v. Marshall Field & Co.,* 93 F.R.D. 438 (N.D. Ill. 1982).

4. Petitioners' Theory Is Contrary to Cases Addressing Implied Conflict Preemption.

The decision below is also consistent with this Court's jurisprudence involving the doctrine of implied conflict preemption. As this Court has made clear in a variety of contexts, a federal law does not impliedly preempt a body of state law where the federal law *says nothing about this subject*. Here, the FAA has no express preemption provision and does not reflect Congress's intent to occupy the entire field of arbitration or contract law. *Volt Info. Sciences, Inc. v. Bd. of Trustees of Stanford Univ.*, 489 U.S. 468, 477 (1989). Instead, the FAA preempts state laws only

if they conflict with the Act's underlying purposes. *Id.* at 477-78. Thus, the FAA preempts state laws singling out arbitration clauses for disfavored treatment because they conflict with the Act's goal of putting these clauses on the same footing as other contracts.[8]

The New Jersey unconscionability and public policy principles applied by the lower Court here address *not* the choice of an arbitral or judicial forum, but the exculpatory rules Petitioners imposed in requiring arbitration. As *Bazzle* demonstrates, the FAA nowhere addresses this subject. Where federal law is silent on a subject, there is no implied conflict preemption of state law based on frustration of federal policy.[9]

C. Petitioners' Policy Arguments Are Unpersuasive.

Petitioners argue for a one-size-fits-all rule of federal law that contract terms banning class actions are always enforceable, so long as they are embedded in an arbitration clause, without respect to the facts of a case or state law. Under Petitioners' view, state law is powerless to regulate such terms no matter how complex the individual claim, how small its value, or how impracticable it would be for individuals to vindicate their legal rights without

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[8] *See, e.g., Casarotto*, 517 U.S. at 686-87 (FAA preempts state statute imposing extra disclosure requirements for arbitration clauses); *Allied-Bruce Terminix Co's, Inc. v. Dobson*, 513 U.S. 265, 280-81 (1995) (FAA preempts state law barring enforcement of all pre-dispute arbitration contracts).

[9] *Cf. Freightliner Corp. v. Myrick*, 514 U.S. 280, 289-90 (1995) ("A finding of liability against petitioners would undermine no objectives or purposes with respect to ABS devices since none exist.").

the class action mechanism. Instead of having courts consider whether a class action ban is exculpatory and thus violates a particular state's generally applicable contract law, Petitioners demand that this Court enunciate a new sweeping rule of federal law that would protect their interests whether or not a given arbitration clause's terms are exculpatory *so that arbitration will never actually take place*. *See, e.g.*, Pet. 20 (arguing that FAA bars fact-based analyses of enforceability under state law).

Petitioners' argument ignores this Court's decisions stating that arbitration is acceptable as an alternative to the civil justice system only where it permits a party to "effectively vindicate" his or her statutory rights. *See, e.g., EEOC v. Waffle House Corp.*, 534 U.S. 279, 295 n.10 (2002); *Gilmer*, 500 U.S. at 28; *Mitsubishi*, 473 U.S. at 637. The Court has never said that an arbitration clause is always enforceable without respect to whether its terms allow for vindication of claims. To the contrary, in *Green Tree Financial Corp. v. Randolph*, 531 U.S. 79, 81 (2000), the Court found that "the existence of large arbitration costs may well preclude a litigant . . . from effectively vindicating [its] rights." In direct contrast to Petitioners' proposed approach, this Court in *Randolph* refused to hold that arbitration is always so cheap that it permits parties to vindicate their rights, or that it is never cheap enough to permit parties to vindicate their rights. Instead this Court required courts to conduct what Petitioners would call "*ad hoc*" fact specific determinations as to whether the costs of arbitration are too high or too low in particular cases.

Petitioners suggest that it is unworkable for courts to conduct a case-by-case determination as to whether a class action ban serves as an exculpatory clause that prevents

parties from "effectively vindicating" their rights in a given case, but this is precisely the kind of analysis that courts regularly conduct. To take the most obvious example, Federal Rule of Civil Procedure 23(b) provides that, for cases where damages predominate over injunctive relief, courts may only certify class actions if – on the facts of those cases – they find that a class action is superior to other methods of adjudicating the dispute. Accordingly, every day in this country, courts evaluate whether individual litigants would be better able (or able at all) to effectively vindicate their claims without the class action device. *See, e.g., Amchem Products, Inc. v. Windsor*, 521 U.S. 591, 617 (1997) ("The policy at the very core of the class action mechanism is to overcome the problem that small recoveries do not provide the incentive for any individual to bring a solo action prosecuting his or her rights.").

Finally, Petitioners' policy arguments are at odds with the FAA itself. As noted, this Court has repeatedly recognized that the FAA incorporates general principles of state contract law. This fact overrides Petitioners' desire for an all-federal FAA, where no variations are permitted between states with respect to contract law. Where, as here, a statute preserves a role for states, that reflects a congressional intent to accept some degree of disuniformity. *Cf. UNUM Ins. Co. of Am. v. Ward*, 526 U.S. 358, 376 n.9 (1999) (disuniform state regulations "are the inevitable result of the congressional decision [in ERISA] to save local insurance regulation.").

In sum, none of Petitioners' arguments based on the FAA merit review.

III. The Petition's Second and Third Questions Likewise Do Not Merit Review.

Petitioners' second and third questions presented addressing the Due Process and Interstate Commerce Clauses are not worthy of review. First, these arguments are waived because neither was timely raised in the state court proceedings. Petitioners did not raise their Due Process Clause argument until they petitioned the New Jersey Supreme Court for rehearing (*see* Pet. F16-20), and did not raise their Interstate Commerce Clause argument until filing their Petition with this Court. In reviewing state court judgments under 28 U.S.C. § 1257, this Court adheres to the general rule that it "will not consider a petitioner's federal claim unless it was either addressed by, or properly presented to, the state court that rendered the decision" under review. *Adams v. Robertson*, 520 U.S. 83, 86 (1997). As the Court explained in *Adams*, "we have generally refused to consider issues raised clearly for the first time in a petition for rehearing when the state court is silent on the question." *Id.* at 89.[10] Since this is precisely what Petitioners did in the state court proceedings with their Due Process question, and Petitioners *never* raised their Interstate Commerce Clause question below, these thirteenth-hour arguments come "too late for consideration here."

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[10] *See also Board of Directors of Rotary Int'l v. Rotary Club of Duarte*, 481 U.S. 537, 550 (1987) ("Appellants did not present the issues squarely to the state courts until they filed their petition for rehearing with the Court of Appeal."); *Radio Station WOW*, 326 U.S. at 128 ("Questions first presented to the highest State court on a petition for rehearing come too late for consideration here . . . ").

Neither of these questions presents a basis for review in any event. In support of their argument that the decision below "denies Petitioners Due Process by retroactively enforcing a new interpretation of New Jersey law" (Pet. 23), Petitioners cite *Bowen v. Georgetown Univ. Hospital*, 488 U.S. 204 (1988), and *Usery v. Turner Elkhorn Mining Co.*, 428 U.S. 1 (1976). *Bowen* held that federal Medicare regulations imposing retroactive cost limits were invalid because they were not authorized by statute, 488 U.S. at 215, while also *upholding* the agency's retroactive application of the rule *in adjudication* on a case-by-case basis. *Id.* at 209. *Turner Elkhorn* upheld a federal statute imposing retroactive liability upon coal mine operators for the death and disability benefits of their injured former workers. *See* 428 U.S. at 18 ("[T]he imposition of liability for the effect of disabilities bred in the past is justified as a rational measure to spread the costs of the employees' disabilities to those who have profited from the fruits of their labor . . ."). The decision below conflicts with neither of these cases because (1) it involves no legislative or administrative rule-making; and (2) its holding invalidating the class-action waiver is grounded in prior New Jersey law addressing terms of adhesion contracts and the necessity of class actions for vindicating small-value claims. *See* Pet. A22-31 (applying unconscionability test set forth in *Rudbart v. North Jersey Dist. Water Supply Comm'n*, 605 A.2d 681 (N.J. 1992)). Petitioners thus fail to raise a substantial Due Process question of retroactivity meriting review.

Petitioners' Interstate Commerce Clause argument meets the same fate. In support of their argument that the decision below "unduly burdens interstate commerce by seeking to impose disparate requirements on arbitration agreements made in the interstate market" (Pet. 25),

Petitioners cite several of this Court's decisions invalidating state laws that *discriminated* between interstate and intrastate commerce. *See Healy v. The Beer Institute*, 491 U.S. 324, 340-43 (1989) (striking down state statute imposing effective price-limit on interstate beer merchants while exempting purely intrastate merchants); *Best & Co., Inc. v. Maxwell*, 311 U.S. 454, 456-57 (1940) (striking down state law imposing tax on hotel room advertisements by any business that is not a regular retail merchant in the state). The decision below does not conflict with or otherwise implicate these cases. The New Jersey Supreme Court applied a general, non-discriminatory standard of unconscionability based on longstanding state-law principles concerning adhesion and exculpation. In arguing that the differences between this and other states' laws gives rise to a Commerce Clause violation (Pet. 27), Petitioners are challenging not merely the decision below but the very existence of state-law regulation of contracts. None of the cases Petitioners cite comes close to supporting this challenge.

In sum, the second and third questions presented do not deserve serious attention.

CONCLUSION

For all the reasons set forth herein, the petition for a writ of certiorari should be denied.

Respectfully submitted,

F. PAUL BLAND, JR.
Counsel of Record
PUBLIC JUSTICE, P.C.
1825 K Street, N.W.,
Suite 200
Washington, DC 20036
(202) 797-8600

MICHAEL J. QUIRK
MARK R. CUKER
WILLIAMS CUKER BEREZOFSKY
210 Lake Drive East, Suite 101
Cherry Hill, NJ 08002

DONNA SIEGEL MOFFA
TRUJILLO, RODRIGUEZ &
RICHARDS
8 Kings Highway West
Haddonfield, NJ 08033

Counsel for Respondent

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No. 06-907

IN THE
Supreme Court of the United States

COUNTY BANK OF REHOBOTH BEACH, DELAWARE AND MAIN STREET SERVICE CORPORATION,

Petitioners,

v.

JALIYAH MUHAMMAD,

Respondent.

On Petition for a Writ of Certiorari to the Supreme Court of New Jersey

REPLY IN SUPPORT OF PETITION FOR A WRIT OF CERTIORARI

Claudia Callaway*
Michael M. Berger
Sabrina M. Rose-Smith
Manatt, Phelps & Phillips, LLP
700 12th Street, NW
11th Floor
Washington, DC 20005

Counsel for Main Street Service Corp.

Marc J. Zucker
Susan Verbonitz
Weir & Partners LLP
Suite 500
The Widener Building
1339 Chestnut Street
Philadelphia, PA 19107

Counsel for County Bank of Rehoboth Beach, Delaware

****Counsel of Record***

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Petitioners County Bank of Rehoboth Beach, Delaware and Main Street Service Corporation respectfully submit this Reply in Support of Petition for Writ of Certiorari to satisfy the Court that it has jurisdiction to hear Petitioners' claim under 12 U.S.C. section 1257(a), and that it also may hear Petitioners' second and third bases for granting the Writ of Certiorari.

Respondent argues that the Court lacks jurisdiction over the New Jersey Supreme Court's judgment, which struck key terms of the parties' arbitration agreement and remanded the case for arbitration consistent with its ruling, but inconsistent with the contract's express, agreed upon terms. Respondent further argues that the Petitioners' second and third bases for granting their Writ—that the New Jersey ruling violates the Petitioners' due process rights and unduly burdens interstate commerce—were not timely raised below and may not be considered.

None of Respondent's arguments calls into question this Court's jurisdiction to grant the Writ. On both points, the Court's exercise of jurisdiction is sound and warranted.

I. THE COURT HAS JURISDICTION TO GRANT THE PETITION BECAUSE THE NEW JERSEY SUPREME COURT RULING IS FINAL WITHIN THE MEANING OF 28 U.S.C. § 1257.

This Court always has given a "practical rather than technical" construction to section 1257, *Cohen v. Beneficial Industry Loan Corp.*, 337 U.S. 541, 546 (1949), using a "pragmatic approach" to determine whether a state court's ruling meets Section 1257's finality requirement. *Cox Broadcasting Corp. v. Cohn*, 420 U.S. 469, 486 (1975). The Court often has found that this practical test requires the Court to exercise jurisdiction in that class of cases where the state court ruling "finally determines claims of right separable from, and collateral to, rights asserted in the

action, too important to be denied review and too independent of the cause itself to require that appellate consideration be deferred until the whole case is adjudicated." *Cohen, supra*, 337 U.S. at 546.

The Court has "recurringly encountered" cases where the state high court has determined a federal issue, but where further proceedings in lower state courts are expected. *Cox, supra*, 420 U.S. at 477. Accordingly, the Court set forth four different scenarios under which the Court would review a state court decision if some part of the action remained to be decided. *Id.* This case presents two of those scenarios.

A. Refusal of immediate review will seriously erode federal arbitration policy.

Without this Court's immediate review of the New Jersey Supreme Court decision, there will be no opportunity to pass on the federal preemption issue. Leaving the New Jersey decision in place and unreviewed has widespread consequences for federal arbitration policy—the core purpose of arbitration will be undermined if review is delayed until after this litigation has run its course. In cases such as this one, the Court's exercise of jurisdiction is necessary and proper.

The Court relied on this *Cox* exception in *Southland Corp. v. Keating*, 465 U.S. 1 (1984), when the California Supreme Court ruled that the state's franchise statute nullified the parties' arbitration agreement, allegedly without violating the FAA. Citing the national policy favoring arbitration, the Court found jurisdiction because "without immediate review. . .. there may be no opportunity to pass on the federal issue and as a result there would remain in effect the unreviewed decision" hostile to the purpose of the FAA. *Id.* at 6.

This Petition presents the same critical question and is subject to this Court's jurisdiction on the same grounds. Petitioners request that the Court review whether the Federal Arbitration Act preempts a state court's attempt to alter an arbitration agreement, if the terms of the agreement to arbitrate expressly preclude class procedure. This very question troubled the Court in *Southland*, but eluded review because it was not properly raised below. *Id.* at 8. The Court has understood the importance of the question raised in this Petition for over 20 years, and its resolution has a substantial impact on the state's power to dictate how arbitrations governed by the FAA will be conducted.

State court rulings challenging the FAA are well suited to review by this Court in order to protect the federal policy favoring arbitration. In *Volt Info. Scis. v. Bd. of Trs.*, 489 U.S. 468, 473 (1989), this Court granted review from a decision refusing to enforce an arbitration agreement under the FAA. More recently, this Court granted review of another FAA case where the Florida Supreme Court issued a ruling hostile to the FAA, and then remanded for further proceedings at the lower state court. *See Cardegna v. Buckeye Check Cashing, Inc.*, 894 So.2d 860 (Fla. 2005)("[W]e quash and remand *Buckeye* for further proceedings consistent with this opinion."), *reversed and remanded, sub nom, Buckeye Check Cashing Inc. v. Cardegna*, 546 U.S. 440 (2006).

Preemption questions merit the same consideration, and are regularly granted review, as are cases where a national policy interest is presented. *See Mid-Con Freight Sys. v. Mich. PSC*, 545 U.S. 440 (2005) (review of a state court decision rejecting the federal preemption defense granted); *see Goodyear Atomic Corp. v. Miller*, 486 U.S. 174, 180 (1988)(finding jurisdiction where review of preemption ruling of Ohio Supreme Court had "important implications" in other states); *see Mississippi Power & Light Co. v.*

Mississippi, 487 U.S. 354, 370 n.11 (1988)(finding jurisdiction of final judgment where "[t]he critical federal question—whether federal law preempts [state proceeding]—has already been answered by the State Supreme Court.), *see also Construction Laborers v. Curry*, 371 U.S. 542, 550 (1963) (Section 1257 does not prohibit the Court from holding as final a state supreme court judgment affirming a lower court's grant of temporary injunction, even where case was still awaiting trial on the merits, "particularly when postponing review would seriously erode national labor policy.").

The Petition before the Court presents an FAA preemption question that necessarily affects, and can substantially alter, the national policy favoring arbitration. As a result, this Court should exercise jurisdiction and would be on firm ground in doing so.

B. Absent immediate review, further proceedings may render the New Jersey decision unreviewable.

The Court should hear this case because the federal preemption, Due Process and Commerce Clause questions presented here will be lost or otherwise not reviewable after further state proceedings.

Petitioners effectively will lose the ability to challenge the New Jersey Supreme Court decision if a class arbitration is completed. No court, state or federal, then will be able to grant the Petitioners more than a Pyrrhic victory. Further, a state appellate court reviewing the arbitrator's decision for abuse of discretion will be bound by the New Jersey Supreme Court ruling, and will not be able to remedy the Due Process and Commerce Clause violations.

In determining finality, "the most important competing considerations are 'the inconvenience and costs of piecemeal

review on the one hand and the danger of denying justice by delay on the other.'" *Gillespie v. United States Steel Corp.*, 379 U.S. 148, 152-53 (1964). The costs of delay in this matter are considerable. *Hughes Tool Co. v. TWA, Inc.*, 409 U.S. 363, 364 n.1 (1973); *id.* at 389-393 & n.10 (Burger, C.J., dissenting) (noting extraordinary expense and inefficiency from failure to resolve threshold issue of federal law, with Court dismissing certiorari and remanding for trial, and then holding that entire litigation was for naught).

Respondent proposes an approach with high cost and potentially irreversible effects on the Petitioners. Class arbitration will severely hinder the low-cost and efficient resolution of Respondent's dispute—the hallmark of arbitration. Class arbitration, if authorized, will require class certification proceedings and class notice. Discovery and pre-merits matters will cost all parties substantial time and money, most of which cannot be saved even if the Petitioners settle to avoid the expense.

Forcing Petitioners to address the time-consuming and expensive class action procedures first, despite a previously negotiated waiver, would render the issue effectively unreviewable. While class arbitration would increase the stakes exponentially over an individual arbitration, any classwide arbitral award would remain reviewable only for fraud, corruption or bias, *see* 9 U.S.C. § 10, or "manifest disregard" of the law, *see Wilko v. Swan*, 346 U.S. 427, 436-437 (1953), overruled on other grounds by *Rodriguez de Quijas v. Shearson/Am. Express, Inc.*, 490 U.S. 477 (1989).

The federal issues may be lost by the time this case reaches this Court again, ***if*** the Petitioners can bear the expense of keeping it alive for that long. *See Kansas v. Marsh*, 126 S.Ct. 2516, 2521 (2006) (finding jurisdiction where Petitioner's issue would be eventually reviewable only

on narrow grounds for appeal that would be inapplicable to Petitioner's case).

The Court must weigh the short delay caused by its review (and anticipated by the Federal Arbitration Act, hereinafter, the "FAA") against the burden and expense of unnecessary potential class arbitration. The former is a recognized cost of favoring arbitration;[1] the latter is a serious burden that should be avoided, particularly if the decision later will be effectively unreviewable.

II. THE COURT HAS JURISDICTION TO REVIEW PETITIONERS' DUE PROCESS AND COMMERCE CLAUSE CLAIMS BECAUSE PETITIONERS PROPERLY RAISED THESE ISSUES BELOW.

Petitioners appropriately preserved their Due Process and Commerce Clause arguments for review before this Court. In *Muhammad*, the New Jersey Supreme Court articulated a new legal principle and applied it retroactively to the Petitioners, thus violating Petitioners' procedural due process rights. *See* App. A at 17-18. (New Jersey Supreme Court expressly noting that the issue of class arbitration "specifically has never before been examined by this Court.").

Respondent's claim that Petitioners waited until the "eleventh hour" ignores the procedural history of this case. The New Jersey trial and appellate court opinions upholding the parties' arbitration agreements had done so under *Gras v.*

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[1] It is worth noting that the FAA, on which Petitioners base their Petition, recognizes that piecemeal litigation may be *required* to effect Congress' stated intent to favor arbitration. *See Dean Witter Reynolds Inc. v. Byrd*, 470 U.S. 213, 221 (1985) ("the relevant federal law requires piecemeal resolution when necessary to give effect to an arbitration agreement").

Associates First Capital Co., 346 N.J. Super. 42, 49-57 (App. Div. 2001), *cert. denied*, 171 N.J. 445 (2002), which had held that a waiver of certain rights in an arbitration clause would be enforced so long as they were sufficiently notorious and specific. Until the New Jersey Supreme Court changed this rule of law, and retroactively applied that ruling to Petitioners, there was no basis for raising the Due Process claim. Once the issue was ripe, Petitioners preserved it for review by raising it in their motion for reconsideration. The motion for reconsideration is reprinted at App. F.

Similarly, until the New Jersey Supreme Court articulated a new "small dollar" rule, its prior jurisprudence on the enforceability of arbitration agreement did not unduly burden interstate commerce by applying a more restrictive state law rule not to all contracts, or even to all arbitration agreements, but only to the narrow class of agreements relating to the procedures available in arbitration, and only to certain entities whose business may generate small dollar consumer claims.

Petitioners raised these issues on motion for reconsideration – the first opportunity to do so – and therefore properly preserved them for review by the Court.

III. CONCLUSION

The Court has multiple bases on which to grant review of the FAA preemption, Due Process, and Commerce Clause concerns presented by this Petition. It therefore should grant review to protect the national policy favoring arbitration, finally resolve the question raised by *Southland*, and protect the due process rights of the Petitioners.

Respectfully submitted,

By: /s/
Claudia Callaway – *Counsel of Record*
Michael M. Berger
Sabrina M. Rose-Smith
Manatt, Phelps & Phillips, LLP
700 12th Street, N.W., Suite 1100
Washington, D.C. 20005

Counsel for Main Street Service Corp.

By: /s/
Marc J. Zucker
Susan Verbonitz
Weir & Partners LLP
Suite 500
The Widener Building
1339 Chestnut Street
Philadelphia, PA 19107

Counsel for County Bank of Rehoboth Beach, Delaware

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